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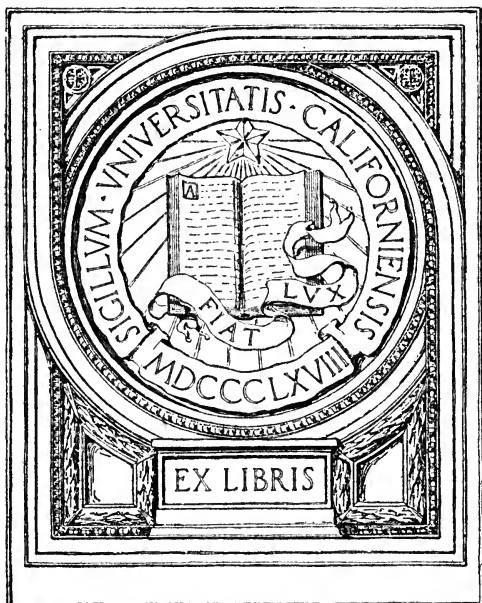
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FEDERAL OPERATION OF TRANSPORTATION SYSTEMS

EXTRACTS FROM HEARINGS

BEFORE THE

COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE
OF THE HOUSE OF REPRESENTATIVES

SIXTY-FIFTH CONGRESS

SECOND SESSION

ON

H. R. 8172



STATEMENT OF

HON. ALBERT M. TODD

PRESIDENT OF THE PUBLIC OWNERSHIP LEAGUE
OF AMERICA

JANUARY 29, 1918



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*Public Ownership League
of America*

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ame

Public Ownership League of America
Albert M. Todd, President,
Westory Building, F & 14th Sts.
Washington, D. C.

**STATEMENT OF HON. ALBERT M. TODD, PRESIDENT OF THE
PUBLIC OWNERSHIP LEAGUE OF AMERICA.**

JANUARY 29, 1918.

Gentlemen, in appearing before you to represent, so far as I may, the interests not only of the Public Ownership League of America but the citizenship at large of our country from whose industry the means have been provided for building and maintaining all of our transportation and other public utilities, I desire first to thank you for the privilege you have so kindly accorded.

At no time in the history of our Nation or the world has legislation been enacted of such colossal economic interest as that now before

Congress, which will so vitally affect the political institutions of our country and the happiness and welfare of its people.

In placing my views before you I shall, on account of the limitations of time, not enter in an academic argument, but confine my remarks largely to the financial aspects of the question. I will only briefly state that public ownership as well as operation of all those utilities and natural resources which by their nature are essentially monopolies, is one of the most natural functions of Government, and is fundamental to justice, equality of opportunity, and democracy. This has been my belief for more than 30 years, and has been constantly confirmed by study and observation in many foreign countries as well as in our own. In reference to this, I will briefly state my experience in the genuinely democratic Republic of Switzerland.

Traveling through Switzerland, one is immediately impressed with the industry, dignity, and liberty-loving spirit of the people, evidenced by their every act and word. The locomotive engineer, the conductor, the fireman, the brakeman, and the men who construct and maintain the tracks know they are not mercenary employees, but are part owners of the railways and all the public works, and as such take a just pride and interest in their duties and labors. Under this system, strikes or lockouts are unknown and impossible, for each employee realizes that in rendering his best service he is rendering a service to the State and, as a citizen of the State, to himself. It will thus be readily seen how with every employee giving his best possible endeavor and each setting an example to those operating the other utilities (in all of which each "citizen-employee" has a personal interest), the State secures much higher efficiency and service, with proportionate decrease in cost to the public. As the fictitious salaries paid in this country to presidents of the public-service companies, whose chief interest is to absorb the earnings of the road are unknown, and all officers and employees are coworkers under civil-service rules—"soldiers for the common good"—private graft and plunder is impossible and unknown.

Illustrating the results under this system, I purchased this ticket which I show you, good for 42 days continuous or intermittent rides at the pleasure of the holder, over any and all of the railways and steamboats, for the equivalent of \$27, or about 67 cents a day. Tickets are also issued for 1, 3, 6, and 12 months at much lower rates; and yet, though these roads, in many places tunneled through the mountains or skirting precipitous cliffs, cost a million dollars per mile to construct, the results are so highly satisfactory that the Republic is constantly building extensions as rapidly as possible.

Results in efficiency and economy equally marvelous as compared with our corporate-owned systems prevail in the telegraph, telephone, express, and street railways; and one wonders how the American people, can be induced in the face of the reckless speculating and plundering of our public utilities by so-called "high financiers," to permit the functions of their life to be thus controlled and abused. It seems incredible that intelligent men engaged in manufacturing and other legitimate business should not join the farmers and wage earners in the demand for public ownership. Under the present corporate system the rule of the railways is to charge "all the commodity will bear," thus limiting both the profits of the producers

and the power of the consumers to buy; the transportation companies thus levying the largest tax possible without entirely killing the industry.

I will now turn to the practical questions involved in the bill under consideration.

The President of the United States, by proclamation issued pursuant to the authority vested in him by Congress, has recently taken over the railroads of the country for operation by the Federal Government during the continuance of the war, in which wise and patriotic act he has had the support and approval of the entire Nation; and as Congress is now legislating respecting the compensation to be paid the railroads, and the various conditions under which these systems are to be operated, it is highly important that in the solution of this question the wisest possible action by Congress be secured.

We who believe that the public ownership and operation of all public utilities which by their nature are necessary to the welfare and happiness of the people are natural governmental functions, also believe that the rightful solution of the question is not based merely upon the operation of these utilities during the period of the war. We look forward to the time—which we hope is in the very near future—when through the patriotism of our citizens and the heroism of our soldiers, victory shall come to our arms, bringing a peace that shall be wise and just to all mankind as the fruit of the great sacrifices America and her allies are making in this world struggle. Among the fruits of such peace those of us who believe in equality of opportunity, civil liberty, and democracy, hope that public ownership and operation of public utilities and natural resources will be among our greatest achievements.

These several circumstances unite to make the present year momentous with respect to the development and solution of transportation problems. Nothing like the present situation has been seen before in the history of the world. No governmental undertaking outside of the great war itself approaches in magnitude either the valuation or the operation of the approximately 250,000 miles of railroads in the United States. The welfare of the country is so obviously bound up with the efficiency of its transportation system and the prosperity of the country is so largely dependent upon the reasonableness of transportation charges that it is needless to dwell upon these general aspects of the problem. But very few people outside of the railroad men themselves appear to realize the tremendous importance of the issues now being determined by the President, Congress, and the Interstate Commerce Commission with respect to the valuation of railroads; the fixing of the compensation to be paid them during the period of governmental operation and private ownership; and with respect to the determination of the just and fair price to be paid by the Government when it shall proceed to Government ownership as well as operation.

The Public Ownership League of America has been organized for the purpose of furthering the policy of Government ownership and operation of public utilities, including transportation systems. It is not blind, however, to the dangers arising out of the stress and strain of these terrible times. It realizes that the mere form of

Government ownership or operation will not in itself guarantee to the people of this country the benefits which they are entitled to receive from the full recognition and performance of the transportation service as a public function. The success of governmental operation of the railroads after the war is over will depend in large measure upon the financial obligations which the Government assumes in connection with their acquisition. Many of the great railroad systems of the country have been exploited and robbed by their managers over long periods of years in ways that have created national scandals unparalleled in the world's history. In this manner many of the roads have at different times been brought to bankruptcy or to a financial condition verging upon it by the studied acts of their officials, who, having been intrusted with the management, have betrayed that trust for their private profit. The Public Ownership League and the thoughtful public at large believe that it would work a gross injustice to the Nation to take the railroads as they are looted and over capitalized, and make good to the owners all of the wicked and foolish speculations of the past, without respect to the actual value of the properties now devoted to railroad purposes. It is not our desire to be destructive in our suggestions as to governmental policies, but rather to be constructive in the best sense, with the future success of Government ownership and operation constantly in view.

Few people outside of Washington realize the enormous one-sidedness of the proceedings before the Interstate Commerce Commission and the committees of Congress. The railroads represent an investment of many billions of dollars and are naturally in a position to employ and do employ great numbers of the most skillful attorneys to take possession of the capital and try to enforce their views and their will upon the governmental authorities having to do with the determination of the great problems at issue. The league believes that the future welfare of the people of the United States will be very greatly affected by the decisions now about to be made with respect to two chief problems, as follows:

1. *The extent of the compensation to be paid by the Government for the use of the railroads during the period of private ownership and Government operation.*—The primary importance of this problem is not in the amount of compensation or rental that may be paid during the continuance of the war or for the brief period of years during which the scheme of private ownership and governmental operation continues, but in the effect that the payment of such compensation and the agreements made with respect to it have upon the ultimate purchase price of the roads when their ownership passes from private hands to the Government. The establishment of a fixed compensation or rental to continue so long as governmental operation of privately owned roads continues will naturally have the effect of determining the earning power of the property from the present time on to the time when the purchase price therefor is to be fixed, and if the compensation or rental is excessive, the result may be the addition of several billion dollars to the permanent burdens of the transportation systems of the country. With the railroads as with public utilities, it is of the utmost importance to the consuming public that the recognized capital value shall be kept as low as practicable and shall not be swelled by the capitalization

against the public of gratuities and special privileges conferred upon the transportation companies in times of great public need and danger.

2. *The principles of valuation to be applied in determining the value of the physical assets of the railroads.*—Valuation is a technical and difficult problem, largely hypothetical, with which the average city is not familiar. Even many well-informed persons suppose that the value placed upon a public utility property by a skillful engineer is an ultimate fact which must be accepted by all parties without question. In truth, however, the final valuation even of the physical property of a railroad or any other public utility is built upon a series of assumptions and by the application of a series of rules with respect to each one of which the particular interests and judgment of the engineers doing the work have great influence. Concealed in a final valuation are many technical questions which are matters of grave doubt and with respect to which the interests of the public and of the public-service corporations are diametrically opposed. As applied to the railroads of the United States, the difference in the principles, advocated at many points in the valuation work, affect the final results to the extent of hundreds of millions or even billions of dollars.

The principles to be applied respecting the capitalization of the railroads in fixing their compensation.—As it will require about three more years for the Interstate Commerce Commission to complete its report on the physical valuations of the railroads, and as the true amounts of money actually and legitimately invested have been so completely hidden by irregular accounting and the burning of books and records to conceal the facts, the true capitalization is at present unknown. On this account I shall introduce herewith evidence and the official findings of the Interstate Commerce Commission to show that the present capitalization as claimed in every case examined is without any vestige of reliability, and is swelled to many times the true amount by extravagance and speculations outside of railroad purposes. In consequence to these facts, I recommend that further investigations be instituted with all speed, with the view of ascertaining the true and legitimate capital investments on which only, and not on water, the Government compensation to the railroads should be based, until the physical valuations be also completed.

In the above connection I respectfully suggest that the willful falsifying of records and the destruction of accounts be included in the section of the bill respecting criminal acts and punished accordingly.

I also respectfully suggest that the bill provide for a continuing lien upon the railroads in favor of the Government for any overpayments which may be made; that the extravagant salaries paid in some instances be revised, and all salaries be based upon the value of the services rendered; that "income on surplus," which is income on income, be eliminated; and that if for temporary purposes it be based on the average income of preceding years, the period should be extended to include the past ten years, rather than for the period proposed of three war years with their excessive profits.

Most important of all the recommendations which I have the honor to submit to you is that Congress shall at the earliest possible

date pass an act providing for the public ownership of transportation systems for the carrying of passengers and freight as well as the telegraph and telephone systems, to accomplish which I am engaged in consultation with practical students of the problem in the drafting of a bill providing for this great step, necessary to the emancipation of the people of this country from the rule of special privilege.

When traveling in France for the first time many years ago, I observed over the entrance of all of their churches as well as public buildings the following motto, which is also the motto of the French Revolution: "Liberty, equality, fraternity." Equality here means equality of opportunity, and when a few are given the right to control the great functions of Government which are thus denied to the general citizenship, equality of opportunity can not exist. There can be no more natural and necessary function of government for promoting general prosperity and happiness than the public ownership as well as governmental operation of all these agencies which contribute to the public good and which by their nature are monopolies. This includes not only the means of transporting passengers, freight, and intelligence, but also means those vast resources of nature as well, which the Almighty placed under the ground for the service of all of his creatures.

Public ownership is also fundamental to democracy, without which civil liberty can not exist.

Herewith I respectfully submit the evidence on which my conclusions are based regarding the finances and practices of the American railroads; and in closing I desire again to express my high respect for the patriotism and forward vision of the President in this crisis.

The illegal and fraudulent practices of the American railway companies in the falsifying of their accounts to cover up the expenditures of the stockholders' money for influencing and controlling legislation, politics, and the press; the frauds practiced by directors in taking for their private use the funds of the company; the deceptive accounting regarding capitalization, investment, etc., and the burning of the books and records to secure secrecy of their acts, as shown in the official reports of the Interstate Commerce Commission.—During the years from 1912 to 1915 various complaints were made by shippers and the public to Congress and the Interstate Commerce Commission respecting certain illegal practices of four important systems of railways and their resulting inefficiency of service and unjust rates. On account of these complaints, which seemed well substantiated, the Interstate Commerce Commission, partly on its own initiative and partly in compliance with resolutions of Congress, made investigations, and issued their official reports of findings, in the years 1913 to 1917, respecting the unlawful practices and financial transactions of the following four railway systems:

The New York, New Haven & Hartford Railroad Co., Report No. 6569; date, July 11, 1914.

The Louisville & Nashville Railroad Co., Report No. 4788; date, February 9, 1915.

The Chicago, Rock Island & Pacific Railway Co., Report No. 6834; date, July 31, 1915.

The Cincinnati, Hamilton & Dayton Railroad Co. and the Pere Marquette Railroad Co., Report No. 6833; date, March 13, 1917.

These investigations were made with the most painstaking care possible, covering long periods of time, in which special agents of the commission were employed to secure information and to investigate the books and accounts, and officers of the companies were summoned before the commission, several thousand pages of testimony being taken. The findings of the commission were published in their official reports mentioned and disclose, among others, the following facts:

The evidence secured by the commission shows that every railroad company investigated knowingly falsified their accounts, partly in order to hide expenditures of large sums for controlling politics and elections and influencing legislation and the administration of laws; falsified the accounts respecting capital, expenses, and profits, so that the commission, in many instances, was unable to find for what purpose vast sums were expended; and in many cases the books and accounts were burned by the directors in order to hide, in so far as possible, various illegal transactions. Many of these acts were done, as the records conclusively show, by directors who are well known as among the world's greatest financiers; yet even though many records were willfully destroyed, the commission was able to secure sufficient evidence in many cases to disclose the names, dates, and facts.

In order to place the various illegal practices in systematic order and to refer to official evidence and the findings of the commission, they may be briefly classified as follows:

1. Extravagant speculations and purchases of worthless securities in the interests of the directors; speculations from the stockholders' money by illegal devices, accompanied by the falsifying of books and accounts and their later burning by the directors.

2. Illegally spending the stockholders' money and property to corruptly influence politics, the press, and public opinion and to secure secrecy respecting their acts.

3. Acts to secure a monopoly against the public interest, by the violation of the laws of many States as well as of the Nation.

4. The organization by the railway directors of "fake" corporations, with "dummy" officers to hide the identity of the real promoters and shield them from prosecution.

5. The voting to themselves by the directors of extravagant salaries, in addition to which large sums were taken by some of these officials without warrant of law.

The various acts recited are necessarily interwoven and will be grouped by subjects as systematically as convenient.

The wasting of the companies' resources in extravagant speculation, and the burning of the records: The following extracts are from the official report, No. 6569, of the Interstate Commerce Commission respecting the New York, New Haven & Hartford Railroad Co., July 11, 1914. All the extracts from the commission's reports respecting the various railway systems are taken verbatim from the records.

Public hearings were held extending over a period of 60 days of almost continuous session. Witnesses in a position to have knowledge of the transactions under scrutiny were examined. In the search for truth the commission had to overcome many obstacles, such as the burning of books, letters, and documents and the obstinacy of witnesses who declined to testify until criminal proceedings were begun for their

refusal to answer questions. The New Haven system has more than 300 subsidiary corporations, in a web of entangling alliances with each other, many of which were seemingly planned, created, and manipulated by lawyers expressly retained for the purpose of concealment or deception. Ordinarily in investigations of this character evidence is easily adduced by placing the witnesses upon the stand, but in this investigation the witnesses other than the accountants for the commission were in the main hostile, and with few exceptions their testimony was unwillingly given.

The result of our research into the financial workings of the former management of the New Haven system has been to disclose one of the most glaring instances of maladministration revealed in all the history of American railroading. In the course of the investigation many instances were uncovered of violation of the laws of different States. As these were not understood to be pertinent to our inquiry under the Senate resolution we did not follow them into their details. As pointing to violations of State laws, we have turned over the evidence concerning local occurrences in New York City to the district attorney for the proper district, and the testimony relating to irregularities in Massachusetts and Rhode Island have been laid before the proper authorities of those States. The commission has also furnished the Department of Justice with a complete record of the testimony.

The difficulties under which this railroad system has labored in the past are internal and wholly due to its own mismanagement. Its troubles have not arisen because of regulation by governmental authority. Its greatest losses and most costly blunders were made in attempting to circumvent governmental regulation and to extend its domination beyond the limits fixed by law.

The subject matter of this inquiry relates to the financial operation of a railroad system which, on June 30, 1903, had a total capitalization of approximately \$93,000,000, of which \$79,000,000 was stock and \$14,000,000 bonds. In the 10 years from June 30, 1903, this capitalization was increased from \$93,000,000 to \$417,000,000, exclusive of stock premiums, or an increase of \$324,000,000. Of this increase approximately \$120,000,000 was devoted to its railroad property and was expended for betterments and equipment. This leaves the sum of \$204,000,000, which was expended for operations outside of its railroad sphere. Through the expenditure of this sum this railroad system has practically monopolized the freight and passenger business in five of the States of the Union. It has acquired a monopoly of competing steamship lines and trolley systems in the section which it serves. The financial operations necessary for these acquisitions, and the losses which they have entailed, have been skillfully concealed by the juggling of money and securities from one subsidiary corporation to another.

SIGNIFICANT INCIDENTS.

Marked features and significant incidents in the loose, extravagant, and improvident administration of the finances of the New Haven as shown in this investigation are the Boston & Maine despoilment; the iniquity of the Westchester acquisition; the double price paid for the Rhode Island trolleys; the recklessness in the purchase of Connecticut and Massachusetts trolleys at prices exorbitantly in excess of their market value; the unwarranted expenditure of large amounts in "educating public opinion"; the disposition, without knowledge of the directors, of hundreds of thousands of dollars for influencing public sentiment; the habitual payment of unitemized vouchers without any clear specification of details; the confusing interrelation of the principal company and its subsidiaries and consequent complication of accounts; the practice of financial legerdemain in issuing large blocks of New Haven stock for notes of the New England Navigation Co., and manipulating these securities back and forth; fictitious sales of New Haven stock to friendly parties with the design of boosting the stock and unload on the public at the higher "market price"; the unlawful diversion of corporate funds to political organizations; the scattering of retainers to attorneys of five States, who rendered no itemized bills for services and who conducted no litigation to which the railroad was a party; extensive use of a paid lobby in matters as to which the directors claim to have no information; the attempt to control utterances of the press by subsidizing reporters; payment of money and the profligate issue of free passes to legislators and their friends; the investment of \$400,000 in securities of a New England newspaper; the regular employment of political bosses in Rhode Island and other States, not for the purpose of having them perform any service, but to prevent them, as Mr. Mellen expressed it, from "becoming active on the other side"; the retention by John L. Billard of more than \$2,700,000 in a transaction in which he represented the New Haven and into which he invested not a dollar; the inability of Oakleigh Thorne to account for \$1,032,000 of the funds of the New Haven intrusted to him in carrying out the Westchester proposition; the story of Mr. Mellen as to the distribution of \$1,200,000 for corrupt purposes in bringing about amendments of the Westchester and

Port Chester franchises; the domination of all the affairs of this railroad by Mr. Morgan and Mr. Mellen and the absolute subordination of other members of the board of directors to the will of these two; the unwarranted increase of the New Haven liabilities from \$93,000,000 in 1903 to \$417,000,000 in 1913; the increase in floating notes from nothing in 1903 to approximately \$40,000,000 in 1913; the indefensible standard of business ethics and the absence of financial acumen displayed by eminent financiers in directing the destinies of this railroad in its attempt to establish a monopoly of the transportation of New England. A combination of all these has resulted in the present deplorable situation in which the affairs of this railroad are involved.

Pages 35 to 41 of the report give a history of the celebrated transaction in which 18 miles of railroad, in which Directors J. P. Morgan, sr., William Rockefeller, and Mr. Miller were interested was unloaded by them on the railroad company at a meeting kept secret from the rest of the board of directors, at which meeting President Mellen presided. This property proved to be more than worthless to the stockholders, having been operated at an annual loss of over \$1,000,000, and for which their directors forced them to pay the vast sum of \$36,434,173.25.

The principal accounts respecting this transaction were kept in the office of J. P. Morgan & Co. in such a manner as to hide the purposes for which moneys were received or expended, under the title of "Special Account No. 2." Part of the accounts were kept by another banker interested in the transaction named Oakleigh Thorne, respecting which the commission report says:

It appeared during the progress of this investigation that the personal records of Thorne which might have shown the details of these disbursements had been burned by him in January, 1912.

This transaction is all the more sensational since the president of the road was not permitted by the directors, who robbed it to the extent of millions of dollars, to know who got the money.

Another startling fact, the exact counterfeit of which may perhaps often have occurred in the history of American railroading, but never before known and published, is revealed in this investigation respecting this road. The record shows conclusively that President Mellen of the road was practically appointed, or selected, at the instigation of J. P. Morgan, sr., and when this "president" desired to ascertain the facts respecting the transaction in which the road was robbed by a conspiracy of Mr. Morgan with three other directors without the knowledge of the rest of the board, "President" Mellen was not permitted by Mr. Morgan to know (as he expressed it over his official signature as disclosed in the record) "Who got the money for the truck turned over."

The following is from the report:

THE NEW YORK, WESTCHESTER & BOSTON RAILWAY CO.

The Westchester is a story of the profligate waste of corporate funds. The road was not necessary as a part of the New Haven system. It parallels other lines already owned by the New Haven and traverses territory which the New Haven already served. That it was recognized as unnecessary by the New Haven itself at its inception is evidenced by the fact that the New Haven sought an injunction to restrain the construction of this road on the specific ground that it was not in answer to any public necessity and paralleled its already existing line.

The enormous sum of \$36,434,173.25 was expended for a road only 18.03 miles in extent, which is being operated at an annual loss of approximately \$1,250,000, and which will have to increase its earnings four and one-half fold before it can pay its operating expenses and fixed charges. It is inconceivable that this enterprise could have been entered into by the New Haven as a result of the mandates of good judgment and proper railroading.

The Westchester acquisition was planned and executed by a special committee of the board, consisting of directors Morgan, Rockefeller, and Miller, with President Mellen as chairman. The vote appointing this committee "on proposed competition between the Connecticut State line and Harlem River, with power," does not disclose an intention to authorize the buying of charters and promotion securities and the building of a new railroad, much less one at a cost of \$36,000,000. It is ambiguous and was evidently intended to conceal a secret purpose. The full board was not taken into the confidence of those directors who wanted these securities purchased, and no report was ever made by this committee placing the situation as they found it before the board.

The first information the board had concerning the extravagant acquisition of Westchester and Port Chester securities was on November 8, 1907, when this committee made its only report. It was then learned that \$11,155,000 had been expended in obtaining control of these two insolvent promotion schemes, and that this expenditure carried with it an obligation to construct two railroads, under franchises of doubtful validity, paralleling the existing line of the New Haven.

There is no record that this committee ever required from these parties an itemized statement of the disbursements they made of the funds advanced from "special account No. 2"; nor was any such statement ever rendered. No vouchers were taken. Special account No. 2 on the books of J. P. Morgan & Co. shows nothing more than the lump sums received from the New Haven and the disbursement of the same to Thorne and later to the Millbrook Co., on notes of the respective payees. It appeared during the progress of this investigation that the personal records of Thorne which might have shown the detail of these disbursements had been burned by him in January, 1912.

In a letter of October 30, 1906, to C. S. Mellen from the attorney, Francis Lynde Stetson, who was representing all the parties in the deal, namely, J. P. Morgan & Co., the Millbrook Co., Perry & Thorne, and the New York, New Haven & Hartford Railroad Co., there is the following language which is significant as to the course the committee was pursuing:

"Referring to the conversation this morning between yourself, Mr. Thorne, and myself, it has occurred to me that it is possible that Mr. Thorne's purchases and even his payments may have to begin before he shall have ascertained the validity of the two principal charters which he is to acquire, and that in the event of the development subsequently of their invalidity it might be that the money spent would be money lost."

The report of this committee, however, was unanimously "approved, ratified, and confirmed" at the meeting of the board of November 8, 1907, at which the following directors were present: Mellen, Rockefeller, Morgan, Milner, Thayer, Brooker, Brush, Warner, Cheney, Miller, Skinner, Barney, Taft, Wittemore, Elton, Hemingway, Robertson, Robbins, and Parker.

After this meeting of the board at which this undetailed report was ratified, Mr. Mellen went to see Mr. Morgan and requested more information as to the expenditure of the amounts. According to Mr. Mellen's evidence, Mr. Morgan asked him if he knew who wrote the report, and upon Mr. Mellen's reply, "Yes; Mr. Stetson wrote it," Mr. Morgan asked him, "Do you think you know more than Stetson"? Mr. Mellen admitted he did not, and apparently acquiesced, but took the precaution to write upon the back of his report, while still smarting under the humiliation of the interview with Mr. Morgan, the following words:

"The trouble with this is there is nothing to show who got the money for the truck turned over. I don't like the looks of it, and I don't see why the matter should not be made plain. If I had the stock and sold it, I should expect others would state they bought it of me; but that don't seem to have been the disposition here. I never have known the first thing about who originally held the securities, what they were sold for, and no one has thought I was entitled to know. Perhaps I am not. I would feel better if there were at least a disposition to let me know something more than appears in the record.

"C. S. M."

* * * * *

There were just thirteen things that had to be done, according to Mr. Mellen, to get the Westchester out of its franchise difficulties, and it is significant that all amendments to the franchises were obtained, and the sequence was that the New Haven, in addition to these things, received 30,431 of the 34,053 $\frac{1}{2}$ outstanding shares of the New York, Westchester & Boston Railroad Co. stock, which Mr. Mellen testified was not worth 10 cents a pound. The testimony is somewhat occult, but the character of the transaction is no less certain. This money was used for corrupt purposes and the improper expenditures covered up by the transfer to the New Haven of these worthless securities.

The committee had kept minutes of its meetings, which were filed with its report, but these show little beyond the authorizations to the president of the New Haven to deposit large amounts from time to time with J. P. Morgan & Co. in an account which appeared on the books of that banking firm as "special account No. 2." The committee made a contract with Oakleigh Thorne and Marsden J. Perry, both presidents of banks which were large creditors of the companies whose securities were to be acquired. The contract authorized and required Thorne and Perry to purchase for the New Haven 66 per cent of the stock of the several companies, and when this was done they were to construct the railroad. The contract is remarkable in that no limit is placed on the amount that might be paid for the securities or expended in building the road, but these parties were to receive, as commission for their services, 7½ per cent of the amount expended.

* * * * *

To this figure, however, must be added the \$14,090,008.18 expended before the construction began, making a total of \$36,434,173.25, which yields the remarkable per-mile cost of \$2,020,752.81.

In providing the money for this construction bonds to the extent of \$17,000,000, sold at a discount of \$1,200,000, were issued on the property, bearing the guaranty of the New Haven. This guaranty has meant a drain on the New Haven resources of \$1,250,000 per annum, since the earnings of the Westchester fall this far short of paying the fixed charges on the property. The president of the Westchester testified that the earnings of his road would have to increase 4½ times before the Westchester will become self-sustaining.

What could have been the motive for unloading the Westchester upon the New Haven at the expense of the stockholders of the latter must be left largely to conjecture. The one accomplished result, however, of the Westchester transaction was the stifling of possible competition into New York City from New England.

The blame for the Westchester rests squarely upon the directors of the New Haven road. Some are guilty for acts committed; others, the greater number, for their failure to act. They are alike culpable and responsible to the stockholders.

Maladministration costs the stockholders over \$20,000,000.—On pages 55 and 56 is the following:

THE NEW ENGLAND INVESTMENT & SECURITY CO.

This company and its affairs constitute a striking illustration of the deliberate attempt to entangle the New Haven with street railways which has recently been publicly avowed by former president Mellen. * * *

The Supreme Judicial Court of Massachusetts (198 Mass., 413) decided in substance that this company was not separate and independent of the New Haven, but was a mere device of that company to continue to hold stock in Massachusetts trolleys in violation of the laws of that State.

The testimony shows that Charles S. Mellen held control of the common stock of this company through James B. Brady, as a dummy, until quite a recent period. These shares have been transferred to Sanderson & Porter, a firm of railroad contractors and builders, who since 1902 have from time to time been engaged in operations for the New Haven.

It seems quite clear, in view of the relations of this firm with the New Haven in the past, that this stock is now held by Sanderson & Porter for the New Haven.

All profits which this company has made in the past have been the result of transactions in the purchase and sale of securities in which the New Haven had title or large interests, not in the open market, but under circumstances which would have been collusive and fraudulent if this security company was in fact an independent organization entirely separate from the New Haven.

On its note there were turned over to it at one time \$9,918,145.65 of securities bought and paid for with New Haven funds.

The inside facts as to its dealings show a continued operation in violation of Massachusetts laws and in flagrant violation of the injunction issued by the highest court of that State.

A summary of the operations of the New England Investment & Security Co., as recorded on its books appears in the appendix, identified as Exhibit D.

Juggling the accounts to increase capitalization and hide irregularities.—It has always been a favorite device of the American railroads to print additional certificates of capital stock which represent no real value, and sell them to the public; and in other cases by the juggling

back and forth of the assets and accounts to suit the private purposes of directors and financiers, to form an excuse for increased rates. The Interstate Commerce Commission refers to these methods in the following extracts from pages 57-58 of the report.

QUESTIONABLE METHODS EMPLOYED TO INCREASE THE AMOUNT OF CAPITAL STOCK.

Increases in capital stock of the New York, New Haven & Hartford Railroad Co. have been made upon the basis of transfers of assets from one subordinate company to another.

The steamship properties of this system at one time were held by the New England Navigation Co., approximating a cost of \$11,500,000. This latter company in 1907 transferred the title to these steamship properties to the Consolidated Railway Co. at a value of \$20,000,000. The Consolidated Railway Co. thereupon increased its capital stock \$20,000,000. The Consolidated Railway Co. was then merged with the New Haven, and the stock of the latter company increased \$30,000,000, \$20,000,000 of which went to the New England Navigation Co., and placing in its treasury by this transaction \$20,000,000 Consolidated Railway stock, which by the merger became New Haven stock, with a market value of over \$30,000,000. It was this stock with which control of the Boston & Maine Railroad Co. was secured.

MANIPULATION OF ACCOUNTS.

Proper accounting demands that the records of a company should reflect accurately the transactions relating to the matter recorded, and where accounts fail to reveal a true history of the transactions it can be due to but one of two causes—carelessness or design.

Several transactions appear of record which show that by no stretch of imagination can the irregularity of recording be classified as due to carelessness; the following are illustrations:

In February, 1911, the New York, New Haven & Hartford Railroad purchased 23,520½ shares of the Rutland Railroad Co.'s stock from the New York Central & Hudson River Railroad Co., giving in exchange therefor its check upon the Farmers' Loan & Trust Co. in the sum of \$2,364,977.15. No entries can be found in the record of the New Haven Co. which reveal this transaction. The stock thus acquired was on the same day, with a check for \$135,022.85, delivered to the New England Navigation Co. in exchange for its note of \$2,500,000. The effect of the recording of this transaction is that the sum paid the New York Central for the stock shows as a cash advance to the New England Navigation Co.

February 14, 1910, the New England Navigation Co. sold, through the firm of J. P. Morgan & Co., 50,000 shares of New York, New Haven & Hartford Railroad Co. stock at a price of 157 net, the cash proceeds amounting to \$7,849,000. A check was remitted by J. P. Morgan & Co. for \$5,162,203.02 to the New England Navigation Co., and 16,744 shares of Worcester, Nashua & Rochester stock were acquired for the account of the New England Navigation Co. at a total cost of \$2,686,796.98.

Dummy companies formed to hide the identity of railroad officials as to their complicity in illegal acts and frauds on the stockholders.—The following is from pages 45, 60, and 61 of the official report:

Witnesses who were officers of some of these companies appeared before the commission and testified that they acted as "dummies" under the directions of Robbins and of attorneys selected by him. Some of them handled, without any knowledge of the nature or purpose of the transactions, checks approximating \$3,000,000.

* * * * *

DUMMY COMPANIES.

The frequency with which dummy corporations and dummy directors appear in this record leads to the conclusion that some one high in the councils of the New Haven had an obsession upon the subject of the utility of such sham methods. The directors of the Billard Co. confessed that they were dummies and knew nothing of its operations. Why men of respectability and standing as these appear to be should lend their names as dummies passes comprehension.

In the organization of one of the steamship companies the young lady stenographer was made president; and a youth of 21 years of age by the name of Grover Cleveland Richards was selected as treasurer of another company.

Clerks and irresponsible persons were drawn upon to supply the demand for dummies in the financial joy riding by the management of the New Haven. Mellen's stock in the New England Investment & Securities Co. was held by James B. Brady, who testified that he was merely a dummy for Mr. Mellen. Director Skinner's stock in this same company was held by a relative and a bookkeeper in his office. Thus, throughout the entire story of deception, the New Haven management vainly endeavored to hide the true facts behind these dummy individuals and dummy corporations.

As a matter of law, such devices are feeble and puerile, but if the master financiers behind these New Haven transactions could use these sham methods and thus give their indorsement to the availability of such crooked schemes to cover the true substance and fact of financial transactions it indicates a low state of financial morality. No condemnation can be too severe to apply to the frequent use of these companies by the New Haven.

While in many States there are safeguards established by law, in other States there is such a prodigality in the creation of corporations as to greatly prejudice the interests of investors, creditors, and the public welfare generally.

While stock in the New Haven road was listed on the New York Stock Exchange a large portion of its funds were invested in "blue sky" corporations, the officers of which knew nothing of the purposes or assets of the companies of which they were managers or officers.

How the officials profited at the expense of their roads by contracts with companies in which they or their friends were financially interested.—The records of the New Haven, as well as the other railway systems investigated, invariably show that the officials did not purchase their supplies in a businesslike manner and at reasonable prices, but at extravagant prices in their own interest without regard to that of the stockholders. As this was the general custom, and the history abounds with many transactions, a single reference must suffice from page 61 of the report.

LARGE PURCHASES WITHOUT BIDS.

Purchases of cars and coal are two large expenditures that railroads make. The New Haven purchased cars almost exclusively from James B. Brady without competition and to the extent of some \$37,000,000. Mr. Brady, as a witness, made no secret of his generosity to the officials with whom he had business. His methods were justified by him on the ground that the officers of the New Haven were old friends.

Locomotives were purchased from a company in which a director of the New Haven was also a director. Many supplies obtained by the New Haven were from companies having directors who were also directors of the New Haven.

Corporate economy is not practicable where gifts and obligations arising from friendship tend to obscure official duty.

The following extract respecting the railroads' expenditures for controlling politics is found on pages 61-62 of the report:

POLITICAL CONTRIBUTIONS.

The New Haven Railroad had no politics. It was Democratic in Democratic States and Republican in Republican States. As Mr. Mellen testified, its effort was always to "get under the best umbrella."

Payments made for political purposes totaled a large sum.

For instance, in 1900, \$50,000 was contributed by the New Haven for campaign purposes through J. P. Morgan & Co. No proper and complete voucher for this payment appears on the books of the New Haven Co.

In 1904 a payment of \$50,000 was made through Mr. Mellen for political purposes. This was secretly done and not reported to the directors or stockholders or in any manner made public.

No public-service corporation may rightfully use corporate funds to promote a political cause or to support a political candidate or a political party.

A corporation as such has no political principles to maintain and no political candidates to support.

The revenues of a public-service corporation are for the most part derived from the exercise of the right delegated to it by the sovereign power to tax the public by fixed rates established in accordance with law. Shippers and the traveling public may be presumed to be divided in political opinion. Corporate revenue derived by public tax from men of one political conviction can not be used to support the fortunes of a candidate or party of contrary political principles.

Regardless of the injustice to stockholders and travelers belonging to another party which results from such use of funds, the withdrawal from corporate use and the diversion to political use is illegal and indefensible.

THE STEAMSHIPS.

The New Haven, from time to time, had felt the harassing effect of competition from the steamship lines that plied between the several larger cities that it served. Restless of any limitation of his power, President Mellen proceeded to acquire the steamship lines and thereby stifle this interference with the New Haven properties.

The Hartford & New York Transportation Co. cost the New Haven \$2,538,916.78; the Eastern Steamship Corporation cost \$4,200,000; the Merchants & Miners' Transportation Co. cost \$5,774,500; the New Bedford, Marthas Vineyard & Pawtucket Steamboat Co. cost \$141,700; the New England Steamship Co. cost \$12,100,000; the Maine Steamship Co. \$17,300, or a total of \$24,772,416.78.

The testimony shows that the physical valuation of the properties acquired as a result of these outlays approximates something like \$10,000,000. The New Haven advises that it has recently disposed of its holdings in the Merchants & Miners' Transportation Co. at a loss of \$3,594,500.

These steamship lines were not acquired by the New Haven openly, but covertly and by devious methods. Dummy companies, and dummy officers and directors were used in financial maneuvering that resulted in the New Haven controlling these steamships.

In connection with these steamship purchases it was necessary to have piers. The record shows money payments in connection with pier leases which were unmistakably improper, and these payments were covered up by being charged on the books of other companies to the New Haven under such headings as "repairs on steamers."

There were payments to one John Hall McKay of many thousands of dollars for which no itemized vouchers were given. Mr. McKay left for Europe after this investigation was commenced, and his evidence could not be secured. These pier leases in the city of New York are controlled by public officials, as the municipality owns the piers and arrangements for the leases had to be made through these officials. But because of the methods employed to conceal these expenditures by increases of capital stock and otherwise, it has been impossible to give any total amount of these payments.

After Mr. Mellen had obtained control of every boat line of any importance in New England he suddenly changed his attitude when the public discovered the real ownership. It was then that he proposed and urged that they be disposed of, but in this he was overridden by his board.

Millions wasted in the purchase at extravagant prices of trolley lines and steamship companies in which transactions a United States Senator and railroad directors profited at the expense of their stockholders.—
The following is from pages 41-44 of the report:

RHODE ISLAND TROLLEYS.

The purchase of the Rhode Island trolleys was another instance of millions wasted in acquiring properties that bring an annual deficit instead of a surplus, and constitute a liability instead of an asset in the New Haven system.

* * * * *

The evidence shows that the Rhode Island trolley transactions were deliberately entered into with a full knowledge of the large deficit that they would bring, and with the determination to acquire trolley control in Providence regardless of expense.

A committee of the board of directors of the New Haven had been appointed for the purpose of looking into the Providence trolley situation, with a view of purchasing that property, and this committee, after considering the proposition, reported adversely. Not content to abide by this action of his board, Mr. Mellen, after some six months, revived the matter. This was done after a conference between Mr. Mellen and former Senator Nelson W. Aldrich, who was largely interested in the United Traction & Electric Co., the largest lessor company.

The United Gas Improvement Co., of Philadelphia, that controlled this property under lease, had capitalized the future hopes of the proposition into a holding company known as the Rhode Island Securities Co. and had issued \$19,899,000 of debentures, which represented an investment of approximately only \$6,000,000. The difference in these amounts was, as Mr. Mellen testified, merely capitalized water.

Not to be deterred by extravagant expenditure, Mr. Mellen undertook to exchange the debentures of the Providence Securities Co., which he had created for the purpose, for these debentures of the Rhode Island Securities Co., and to add thereon the guaranty of the New York, New Haven & Hartford Railroad Co., both as to principal and interest. The result of the transaction was to enable the United Gas Improvement Co. to realize par value on these securities based merely upon lively expectation of future possibilities, and thereby immediately placed the burden of the watered stock upon the backs of the New Haven stockholders.

The millions that were made from this transaction did not come through magic, but were brought into existence at the expense of the stockholders of the New Haven, upon whom and the public the yoke of giving value to these securities ultimately rested, and the New Haven stock was diluted to the extent of the water thus added. This gas company also owned some Connecticut trolley lines, and it was made a further condition of the Rhode Island trolley acquisition that the New Haven take over these properties.

When the details had been worked out by Mr. Mellen for the assuming of this additional burden the board of directors without question acquiesced. Mr. Mellen testified that these Connecticut trolleys represented a payment of about \$10,000,000 more than their value.

This transaction seems such an extravagant purchase as makes it a matter of interest just who owned the securities of the Rhode Island Securities Co. This information could be furnished from the stock books of that company, but during the progress of this investigation it was learned that these books had also been burned. A detailed report on the Rhode Island trolleys is to be found in the appendix made a part hereof, Exhibit B.

The Rhode Island and Connecticut trolley ventures are further evidences of the prodigality in the expenditure of the money of the New Haven stockholders in carrying out an unlawful policy of transportation monopoly.

Losses of \$60,000,000 to \$90,000,000 due to waste, mismanagement, and speculations by railroad officials, and attempts to control politics, the press, and public opinion.—The following is from pages 63–70 of the official report:

There is the additional loss growing out of the unfortunate Billard transaction of \$2,748,700 unless John L. Billard is compelled, as he should be, to make restitution.

In addition there have been large expenses incurred in litigation, in procuring legislation, and in a vain attempt to stem the tide of adverse popular opinion.

* * * * *

The annual deficit to the New Haven from bond interest, interest on other obligations, and taxes resulting from the Westchester venture amounts to \$1,179,243.92. When the operating deficit is added, the total annual loss to the New Haven is \$1,657,241.99.

* * * * *

These annual losses will, to a large extent, recur from year to year for an indefinite period, and therefore represent large future losses.

From all of the foregoing and from a careful consideration of the method in which expenditures, not specified herein, have been made, it is submitted that a reasonable estimate of the loss to the New York, New Haven & Hartford Railroad Co. by reason of waste and mismanagement will amount to between \$60,000,000 and \$90,000,000.

The splendid property of the New Haven Railroad itself will be called upon for many a year to make up the drain upon its resources resulting from the unpardonable folly of the transactions outside the proper field in which stockholders supposed their moneys were invested.

But honesty and efficiency of management of this property as a railroad only will undoubtedly, in time, restore its former standing.

EVIL OF INTERLOCKING DIRECTORATES.

A system of interlocking directorates has grown up and flourished in the past few years which has brought about combinations and intercorporate relationships not conducive to the public welfare. On the New Haven board of directors there was a

representative of the Pennsylvania Railroad, which railroad owned 35,000 shares of New Haven stock; there was a representative of the New York Central, which owned 35,000 shares; there was a representative of insurance interests that owned 35,000 shares and a representative of an express company that had a contract with the railroad; there were directors who were also directors of the Standard Oil Co., the United Steel Corporation, the Pullman Co.; in fact, every other interest seemed better represented on the New Haven board than the average stockholder's interest.

After an exhaustive investigation of this great railway property the commission summed up its findings as follows:

NEW HAVEN MONOPOLY CORRUPT.

This investigation has demonstrated that the monopoly theory of those controlling the New Haven was unsound and mischievous in its effects. To achieve such monopoly meant the reckless and scandalous expenditure of money; it meant the attempt to control public opinion; corruption of government; the attempt to pervert the political and economic instincts of the people in insolent defiance of law. Through exposure of the methods of this monopoly the invisible government which has gone far in its efforts to dominate New England has been made visible. It has been clearly proven how public opinion was distorted; how officials who were needed and who could be bought were bought; how newspapers that could be subsidized were subsidized; how a college professor and publicists secretly accepted money from the New Haven while masking as a representative of a great American university and as the guardians of the interests of the people; how agencies of information to the public were prostituted wherever they could be prostituted in order to carry out a scheme of private transportation monopoly imperial in its scope.

DIRECTORS CRIMINALLY NEGLIGENT.

It is inconceivable that these wrongs could have gone on without interference if the members of the board of directors had been true to the faith they owed the stockholders. A number of directors appear in many instances to have voted without knowledge and to have approved the expenditure of many millions without information. According to the testimony of some of the directors they merely approved what had been done by some committee or by some officer of the company. The directors' minutes reveal that it was largely a body for ratification and not authorization as the law intended a board of directors should be. None of the directors would have been so careless in the handling of his own money as the evidence demonstrates they were in dealing the money of other people. The directors actively or passively acquiesced in the efforts of the Mellen-Morgan-Rockefeller régime to extend the domination of this corporation over the whole transportation field in New England.

If these directors who were faithless to their stewardship were held responsible in the courts and at the bar of public opinion for the failure to do those things they should have done, the lesson to directors who do not direct would be very salutary.

Most of the directors of the New Haven accepted their responsibilities lightly. They failed to realize that their names gave confidence to the public and that their connection with the corporation led the public to invest. When these directors were negligent and serious losses resulted therefrom they were guilty of a grave dereliction of duty and a breach of trust that was morally wrong and criminal in its fruits.

Directors should be made individually liable to civil and criminal laws for the manner in which they discharge their trust. A corporation can be no better or worse than those who operate it. It should be just as grave a crime to plunder stockholders or the public through a railroad corporation as it is to personally rob an individual.

SUBSIDIARY CORPORATIONS CONDEMNED.

It was found in the investigation of the New Haven system that there were 336 subsidiary corporations, and the books of the New Haven road proper reflect only a small part of the actual financial transactions of the railroad. Many of these subsidiary corporations served no purpose save an evil one. They were used to cover up transactions that would not bear scrutiny and to keep from the eyes of public officials matters that were sought to be kept secret. The commission should have the power to examine not only the books, records, papers, and correspondence of interstate carriers but of subsidiary companies as well.

REMEDY IN PUBLIC CONSCIENCE AND LAWS.

The insuring of honesty throughout the management of the great railroads of the country is a most important question before the people to-day; and only when, through exposure of wrongdoing and an awakened public conscience, coupled with effective laws, this result is produced may railroading be placed upon the high level that it should occupy. The revelations in this record make it essential for the welfare of the Nation that the reckless and profligate financiering which has blighted this railroad system be ended, and until this is fully done there will be no assurance that the story of the New Haven will not be told again with the stockholders of some other railroad system as the victims.

THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY CO.

Having reviewed some of the principal transactions of the New York, New Haven & Hartford Railroad Co. in defrauding its stockholders and the public, extracts will now be submitted from the official report of the Interstate Commerce Commission, No. 6834, dated July 31, 1915, entitled "In re Financial Transactions, History, and Operation of the Chicago, Rock Island & Pacific Railway Company."

Owing to the limits of space available in this statement to Congress, and having gone into the transactions previously investigated in considerable detail, we will content ourselves with brief extracts from the official report just mentioned, which, when read in full, discloses a duplication of the illegal acts of the other systems investigated, together with some new details respecting the salaries of its officers and the manner in which they abstracted, for their private uses, from the company treasury large sums without accounting therefor. The same system of false accounting, extravagance, waste, and the use of the stockholders' money for controlling politics and the press and for other illegal acts is found in the official report of the commission.

The result of these illegal practices was to reduce the value of the stock, which in 1902 was \$200 a share, to \$20 in 1914, and to put the road in the hands of a receiver—all in the private interest of a minority of its directors, without the knowledge of the rest of the board, for the purpose of further exploiting the stockholders.

Among the acts so startling and sensational as to vie in interest with the wildest fiction may be mentioned the following:

The chairman of the executive committee, L. F. Loree, in addition to a salary of \$75,000 per annum, demanded and received a contract giving him a present or "bonus" in an additional sum of \$500,000 after the expiration of his five-year contract. Owing to trouble which arose between him and the rest of the board after only 10 months' service, he was given a "bonus" of \$450,000 to quit the job, so that his compensation for 10 months exceeded \$500,000.

A majority of the officers took money from the company's treasury whenever they desired without warrant of law or without specifying the purpose the money was to be used for. A stockholder who brought suit to secure an investigation and an accounting of the acts of the directors was paid \$217,000 to relinquish his suit in order to keep these facts from public knowledge.

The following extracts from the official report of the commission giving a sketch of the system, the methods by which the directors squandered the funds of the stockholders in extravagance, specula-

tion, and dishonesty; and the conclusions of the Interstate Commerce Commission are found on pages 43 to 61 of the report.

In 1902 the main line of the Chicago, Rock Island & Pacific Railway Co. extended from Chicago to Denver, with branch lines to St. Paul, Minneapolis, and Kansas City. The territory served is one of the richest and most prosperous in the country and the system's ramification of branch lines insures to it a large volume of tonnage. It was then thriving and its prospects were promising, its stock selling in the markets of the world at more than \$200 a share. In 1914 the shares had fallen to \$20 and the road is now in receivers' hands. The evidence shows that the earnings of the railway company have steadily increased, and that in 1914 they were the largest in its history.

On June 4, 1902, the capital stock of the railway company was increased to \$75,000,000 and the board authorized President Leeds to sell to certain individuals portions of this increased stock at par, although at the time the stock was quoted on the market above 175.

The original articles of consolidation provide that the maximum of indebtedness to which the company might subject itself should not exceed two-thirds of its outstanding capital stock. This maximum has been increased from time to time until the funded debt of the railway on June 30, 1914, was \$238,746,000, an increase of nearly \$175,208,000 over the amount outstanding on June 30, 1901. On June 30, 1914, the total capitalization of the railway company was \$313,741,000. Of this amount only \$75,000,000, or 28.73 per cent, was capital stock on which dividends might or might not be paid, according as the net earnings of the company might or might not warrant. The remaining 71.27 per cent of the total capitalization consisted of interest-bearing debt, including \$3,500,000 of short-term loans, on which interest was required to be paid regardless of earnings.

In 1902 plans were laid by five directors to form a syndicate and holding company and secure control of the road to plunder and to wreck it.

The following is from the official record:

SYNDICATE CONTROL.

In 1901 Daniel G. Reid, W. H. Moore, J. H. Moore, and W. B. Leeds purchased about \$20,000,000 of stock of the company, and by the use of proxies they soon became members of the board of directors, W. B. Leeds being made president and D. G. Reid chairman of the executive committee. This syndicate procured the selection of other members of the board of directors, notably F. L. Hine, George McMurtry, and George T. Bogges, each of whom appears to have acted and voted in accordance with the wishes of the members of the syndicate. One other director stated that he knew but little of what was being transacted in the affairs of the railway company, and that he was a member of so many other boards of directors that he had no opportunity to examine into things for himself, but had to take the word of those in authority. Thus the syndicate controlled the board through the directorships held by themselves and by those subject to their wishes.

ORGANIZATION AND USE OF HOLDING COMPANIES.

In July, 1902, the syndicate organized two holding companies, the Chicago, Rock Island & Pacific Railroad Co. of Iowa, and the Rock Island Co. of New Jersey. The railway or operating company will be referred to hereinafter as the railway company, and the holding companies as the Iowa company and the New Jersey company, respectively. The St. Louis & San Francisco Railroad Co. will be referred to as the Frisco.

The directors paid a large sum to have a suit suppressed which would have exposed their illegal transactions. Upon page 46 occurs the following:

A significant transaction at this time is that growing out of the action of C. H. Venner, a stockholder of the railway company. He made demands upon the officers of the railway company in December, 1902, and in January, 1903, for a list of its shareholders. Being ignored, he instituted on January 31, 1903, a proceeding in a State court of Illinois to enjoin the organization of the holding companies and the exchange of railway company stock for their securities. In February and March, 1904, the railway company paid Venner \$291,000, ostensibly in consideration of his delivery

to it of securities of the New Jersey company and of the railway company valued at \$91,000 and stock of the Nebraska Central Railway and of the Nebraska Construction Co. of a nominal value of \$200,000. Thereupon the suit to restrain the holding companies' plan was dismissed. Neither the Nebraska Central Railway Co. nor the Nebraska Construction Co. had any road or other tangible assets, and their stock is therefore considered to be without value. The conclusion is obvious that the payments to Venner were in consideration of his refraining from further prosecuting in the courts his opposition to the syndicate plans. The railway company incurred in this litigation expenses amounting to about \$17,000.

Compensation and peculations of officers who defend salaries of \$50,000 to \$75,000 for themselves, but assign the wages of clerks, telegraph operators, conductors, and brakemen as the reason for the financial troubles of the road.—On pages 47–50 is the following:

SALARIES OF AND CONTRIBUTIONS TO OFFICERS AND DIRECTORS.

The salaries paid to some of the principal officers at various periods were as follows:

	Per annum.
H. U. Mudge, president.....	\$60,000
L. F. Loree, chairman executive committee (one-half to be paid by the Frisco).....	75,000
R. A. Jackson, vice president and general solicitor.....	50,000
R. R. Cable, member of board of directors.....	32,000
W. B. Leeds, president.....	32,000
B. L. Winchell, president.....	40,000
B. F. Yoakum, chairman executive committee.....	30,000
Daniel G. Reid, chairman board of directors.....	32,000
C. H. Warren, first vice president.....	35,000

W. G. Purdy, upon his retirement from the presidency, was given two years' salary at \$22,500 per annum.

Mr. Mudge, president of the railway company and now one of the receivers, asserted that the troubles of the railway were in a measure due to increase of wages and governmental regulations. When asked what wages he referred to as being increased he pointed out the wages of clerks, telegraph operators, conductors, and brakemen. While he regarded the wages of these minor employees as having partially sapped the financial strength of the railway, he declared that the salaries paid to the higher officers of the company had no appreciable effect on its expenses.

D. G. Reid, upon the witness stand, was interrogated and answered as follows:

"Question. Mr. Reid, do you think these men earned these high salaries?"

"Answer. I do not think there is a man who did not earn more than he was getting."

"Question. In other words, you defend paying these high salaries?"

"Answer. I defend nothing. Here is 8,000 miles of railway; a man who can run 8,000 miles of railroad is worth all he can get."

Many large contributions were made to officers and directors of the railway company. George T. Boggs, a director and secretary to the board of directors of the railway company, and also a director in the two holding companies, admitted that he served in these capacities merely as a dummy for the syndicate. On the question of the right of the public to have corporate funds of common carriers properly applied, he testified as follows:

"Question. Do you consider that the directors of a railway company, a public service corporation, have the right to do whatever they please with the money of the railway company?"

"Answer. As in their judgment seemed right; yes."

"Question. Did it ever occur to you that the money in the treasury of the railway company was the result of taxation of the public in passenger and freight tariffs, and that the public had an interest in the funds in the treasury?"

"Answer. I don't know that I ever thought of it particularly."

"Question. And that the public had a concern in the funds of the railway company not being dissipated in order that they might be applied to improvements and betterments and to proper purposes?"

"Answer. I never considered that they were dissipated."

"Question. And did it ever occur to you that in taking money from the treasury of the railway company, a public-service corporation, an additional burden was placed upon the passenger and freight traffic in order to make good the loss?"

"Answer. No; I never thought of it in that light."

"Question. You don't believe it now, do you?"

"Answer. No."

This opinion was also expressed in effect by other officers and directors. It appeared to be the idea of those in control of the railway that it was no concern of the public what became of the corporate funds so long as rates were reasonable. Those stating this opinion apparently did not take into consideration the fact that if the funds derived from transportation services are expended wastefully or corruptly the inevitable result must be either increased charges in order to enable the railway company to obtain money to pay operating expenses, or bankruptcy.

Following are specific instances shown of record of the contributions referred to:

J. E. Gorman, first vice president in charge of freight and passenger traffic, was secretly paid \$18,750 per annum, making his total compensation \$43,750, whereas the pay roll showed \$25,000.

C. A. Morse, chief engineer, received a salary of \$15,000 per annum and a secret bonus of \$3,000 on the first of each year.

Upon the retirement of R. A. Jackson as general solicitor he was given \$100,000 in cash.

As an inducement to L. F. Loree, chairman of the executive committee, to relinquish, after 10 months' service, a joint contract with the railway company and the Frisco under which he was to receive a salary of \$75,000 per annum for a period of five years and in addition was to be paid a bonus of \$500,000 at the expiration of the contract, he was given bonds of the railway company of a par value of \$450,000. This was borne equally by the two companies, and the proportion of the railway company was charged to profit and loss. The total amount borne by the railway company in this transaction exceeded \$250,000.

C. H. Warren, vice president, was given by the railway company \$150,000 in par value of the common and \$105,000 in par value of the preferred stock of the New Jersey company and \$50,000 in cash. There was no board authorization for the latter expenditure, the item being represented in the records of the railway company merely by a voucher signed by D. G. Reid.

R. R. Cable, a member of the executive committee, received from the railway company \$30,000 in bonds of the Iowa company, then worth \$24,500, for his services in the acquisition of the Burlington, Cedar Rapids & Northern Railway Co., and he was paid by the latter company \$85,000 in the same transaction. Mr. Cable also received another contribution, which will be referred to later.

Robert Mather, vice president, was given \$25,000 in cash.

George T. Boggs, director and secretary of the board of directors of the railway company, was given \$15,000 in cash when he retired from the secretaryship of the railway company.

As hereinbefore indicated, when the capital stock of the railway company was increased to \$75,000,000, shares of the par value of \$880,500 were placed in the name of the president, to be thereafter distributed in accordance with the following resolution of the executive committee passed at a meeting held in New York July 1, 1902:

"Resolved. That such portion as the president may determine of the shares of the increased capital stock of the company not required for the purpose of the foregoing resolutions shall be disposed of at par by the president for the benefit of such officers of the company as the president shall elect and determine."

This stock was later exchanged for securities of the Iowa and New Jersey companies in the same manner as was stock of the stockholders of the railway company.

Following this exchange R. R. Cable received securities of a market value of \$368,300 for which he paid \$200,000.

H. A. Parker, first vice president, received securities then worth \$27,900 for which he paid but \$15,000.

Robert Mather received securities of a market value of \$145,912 above his payments therefor.

The contributions to officials of the railway company in excess of their salaries aggregated about a million dollars.

IRREGULAR VOUCHER PAYMENTS.

Unexplained vouchers for amounts aggregating \$72,523.45 were disbursed to the officers of the railway company for purposes not clearly defined. One such voucher for \$6,823.12 was drawn apparently to reimburse W. H. Moore for losses sustained by him in "supporting the market while bonds of the railway company were being sold." The voucher was certified by D. G. Reid, "for the benefit of the railway company." No papers were attached to the voucher and no other information was available with respect to the disbursement.

Another voucher in favor of the Liberty National Bank of New York City, in exchange for a cashier's check issued to Robert Mather for \$25 000, is charged to "general expenses" under "operating expenses." This voucher refers to a miscellaneous file shown by the index thereto to have comprehended "contributions to campaign committee." The file, however, was not produced, and a diligent effort on the part of the accountants to secure it was unavailing. Without this file it is impossible to state the purpose for which the money was expended, but the generalization "contributions to campaign committee," in the light of the practices indulged in by the syndicate in question, is clearly suggestive.

The books of the railway company reveal payments aggregating \$44 066.05 to the Denver Post. The vouchers attached read, "for advertising in editorial and news columns." Other entries show that three of these vouchers, aggregating \$20 000, cover a refund that this newspaper received at the rate of 25 cents per hundred on its freight carried over the lines of the railway company from points in Wisconsin.

Another voucher is for \$50,000 to S. M. Felton for the railway's proportion of amount "paid by E. H. Harriman and his associates for money expended by them to secure the discontinuance of a line of road being constructed in 1900 between Peoria, Ill., and Clinton, Iowa, as per agreement between R. R. Cable, chairman of the board, and E. H. Harriman."

AGGREGATE OF LOSSES.

The aggregate losses sustained by the railway company in connection with the foregoing transactions may be summarized as follows:

Expenses of maintaining and housing holding companies, more than...	\$290,000.00
Frisco deal, approximately.....	6,500,000.00
Alton deal, approximately.....	6,370,000.00
Trinity & Brazos Valley Ry. deal, more than.....	4,500,000.00
Consolidated Indiana and Dering Coal Cos., at least.....	1,500,000.00
Contributions or gratuities to officers and directors, about.....	1,000,000.00
Venner transaction.....	217,000.00
Miscellaneous and unexplained expenditures.....	72,523.45

These items show an aggregate loss to the railway company of more than \$20,000,000. In addition thereto it is to be noted that prior to June 30, 1914, the railway company paid to financial institutions, in connection with the issuance of bonds, commissions aggregating more than \$1,600,000 and suffered discounts of more than \$17,700,000.

INDIVIDUAL PROFITS OF PROMOTERS, OFFICERS, AND DIRECTORS OF THE HOLDING COMPANIES.

The amount of gains accruing to W. B. Leeds, D. G. Reid, W. H. Moore, and J. H. Moore through their control and manipulation of the railway company are probably not ascertainable. Reid, when interrogated with a view to ascertaining his profits from the various transactions, explained that he always burned his books at the end of each month.

The quotations placed in the record from the stock market of the New Jersey company stock and the railway company stock showed wide fluctuations. Whatever have been the gains realized by these persons, it is certain that the present holders of the stocks and bonds of the holding companies have that which is of little or no value.

REPORTS TO STOCKHOLDERS.

Misrepresentation of assets in reports to stockholders appears to have been a practice of the directors of the railway company. On June 30, 1904, a book surplus was claimed for the railway company of \$22,343,955.26. By June 30, 1914, the company conceded a reduction of this surplus to \$6,199,841.08, and even this amount was fictitious.

* * * * *

The directors also reported as assets the 5 per cent debenture bonds of the Iowa company, which were in fact worthless, but which were reported as worth nearly \$6,000,000.

In view of the fact that the reported value of the "securities" listed for the year 1914 was nearly \$18,000,000 in excess of their actual value, instead of a surplus of more than \$6,000,000, claimed by the railway company, there should have been shown a deficit of over \$11,600,000.

Another misleading and objectionable practice of the railway company officials was the failure to state on the pay roll the true amounts paid to its officers.

The publication of misleading reports to stockholders can not be too severely condemned, and the individuals guilty of such acts should be subject to adequate penalties.

The bankrupting of railways in the United States has invariably occurred from maladministration and speculation on the part of the officers in charge, and never because of insufficient revenues when wisely and honestly administered. Receiverships have always resulted from the above cause or else have been planned by directors for their own private gain. In some cases the condition of the companies did not warrant receiverships, even though the directors had placed their companies in an embarrassing condition. The receivership of the Rock Island system is an example of the cause last mentioned, and was planned without the knowledge of the majority of the board by a conspiracy of a few directors in which they were joined by the chief counsel of the company, who afterwards acted as receiver in their interest. "Fake" legal proceedings were had through attorneys employed fraudulently to prevent the stockholders defending their rights.

The following is taken from the official report:

RECEIVERSHIP.

The syndicate decided to put the railway into a receivership. The general counsel of the railway company at the suggestion of W. H. Moore, a member of the syndicate, drew the bill asking for a receivership and engaged an attorney ostensibly to represent the other side. The bill was placed in the hands of this attorney with the name of the complainant omitted and he was instructed by the general counsel to locate some creditor of the railway company willing to act as complainant. There was an agreement between the general counsel and this attorney as to the parties the latter would recommend to the court as receivers, the general counsel agreeing to instruct the attorney appearing for the railway company to acquiesce in the recommendations so made.

The board of directors of the railway company was not informed of the intention to file a bill for receivership and at no meeting of the board was any authority ever given for such action. Members of the board of directors not in the confidence of the syndicate were kept in ignorance of the fact that such a bill had been prepared. The stockholders had no information of the purpose to put the railway company into a receivership, although a stockholders' meeting was held after the date upon which the receivership bill was completed by the general counsel, and this general counsel attended the meeting. According to the testimony, the bill was completed by the general counsel March 29, 1915, and the fact that it was to be filed whenever desired by those in authority was known only to certain insiders. The testimony clearly establishes the fact that the railway company could easily have paid the debt of \$16,000 upon which the receivership application was based, and that arrangements probably could have been made to meet all pressing obligations of the railway company.

The creditor at whose instance the receivership application was filed appeared as complainant by request. R. P. Lamont, the president of the American Steel Foundries, the complainant, testified that he would not have thought of bringing such a proceeding against the railway company unless he had understood that it would be regarded as not unfriendly but as a friendly act to oblige the railway company. He only consented that his company should appear as complainant when he was assured that this course was in accordance with the wishes of the railway company and that his company was not to have any care or expense in the preparation of papers or payment of counsel fees. The suit was not a bona fide proceeding to collect a debt, but was instituted to carry out the purposes and schemes of the syndicate controlling the railway.

N. L. Amster, who was elected to the board of directors of the railway company by the minority stockholders at the stockholders' meeting held in Chicago, April 12, 1915, believing, according to his testimony, that no sincere effort was being made by other members of the board to finance the obligations of the railway, undertook to assist in raising about \$6,000,000 needed by the railway to meet obligations soon thereafter to mature. On April 16, 1915, he met and conferred with Messrs. James,

McLean, and Schumacher, all directors of the railway and members of the executive committee, and discussed the company's finances. These three expressed approval of his purpose to negotiate for the money. Amster testified that he had secured assurances for the furnishing of the money from responsible Boston bankers on securities which the railway company had. When he arrived in New York on the morning of April 20 to report this fact he went to the office of the railway company, and, quoting his testimony, "could not find anybody there that would say anything, except a lot of people moving back and forth. I left the office and found on the ticker that the Rock Island had been put in the hands of a receiver." This, Amster testified, was the first information he had of the receivership or that such a step was in preparation, yet he was a director of the road and after the stockholders' meeting in Chicago, April 12, traveled from Chicago to New York with Roberts Walker, the general counsel of the railway company.

It will be remembered that the bill was completed by the general counsel on March 29, this fact being known only to a special few.

The bill was filed April 20. The records of the New York stock market reveal that the railway stock was inactive until the day this bill was completed, March 29. Then the stock began to be largely dealt in, and the price increased from \$20 to \$39 a share. When the bill was filed and receivers were appointed the stock dropped from \$39 to \$20 a share.

It is a forceful commentary on the methods by which a great railway may be manipulated into a receivership, when it is noted that the general counsel, after drawing the bill for a receivership, sold his stock, and the local counsel, who represented the railway company in the receivership proceedings owned no stock in the railway company, and that none of those directly participating in the receivership proceedings had any financial interest in the railway company. The real owners of the railway, the stockholders, the security holders, and the directors, except those composing the syndicate and in its confidence, were in ignorance of the receivership application. Mr. Mudge, former president of the railway company, is one of the receivers.

The general counsel for the railway company, who planned the receivership in obedience to the will of the syndicate, is now counsel for the receivers.

SUMMARY AND CONCLUSION.

This review, giving a brief glance at the wild speculations, frauds, and conspiracies of the officials to plunder and wreck the properties intrusted to their care and place heavy burdens upon both the stockholders and public, needs no further commentary than the closing words of the Interstate Commerce Commission in its report:

The property of the railway company will be called upon for many years to make up the drain upon its resources resulting from transactions outside the proper sphere in which stockholders had a right to suppose their moneys were invested. This record emphasizes the need of railway directors who actually direct. There are too many passive directors who acquiesce in what is being done without knowledge and without investigation. A director of a railroad is a quasi public official who occupies a position of trust. A director who submits blindly to the exploitation of his company is a party to its undoing and he should be held responsible to the same extent as if he had been a principal instead of an accessory before the fact. The greater his prominence the greater his responsibility and the greater his dereliction. Obviously a man of large affairs could not attend to all the details in intricate transactions, but it is inconceivable that a director of ordinary business prudence and sagacity would sanction large expenditures without an inquiry as to the purposes of such disbursements. So long as this situation exists, however, it suggests the need of a law to charge such directors with individual responsibility for the dissipation of corporate funds.

The Clayton Antitrust Act, which becomes effective October 15, 1916, will make it unlawful for any person at the same time to be a director in two or more competing corporations, any one of which has a capital, surplus, or undivided profits aggregating more than \$1,000,000, but common carriers are expressly exempted from its application. It should be just as grave an offense for an official of a railway to be faithless to his trust for financial gain as it is for an elected official of the Government to betray his trust for money reward.

THE LOUISVILLE & NASHVILLE RAILWAY SYSTEM.

This railway system was investigated by the Interstate Commerce Commission. The results of its investigation are to be found in the official report of the commission No. 6319, dated February 16, 1915, entitled: "In re Financial Relations, Rates, and Practices of the Louisville & Nashville Railroad Co., the Nashville, Chattanooga & St. Louis Railway, and other Carriers."

This investigation was the result of a resolution of the United States Senate, prompted by complaints of the public respecting illegal acts of the above company and its subsidiaries, in which it requested the Interstate Commerce Commission to inquire into the financial affairs and capitalization of the company, its practices, and its efforts to illegally influence or control politics, legislation, and public opinion.

Because of the fact that some of the records and accounts of the company had been burned by them and the further fact that the commission was permitted by the company to inspect but part of those which remained, and the further fact that the officials of the road and other witnesses summoned to appear before the commission refused to testify, the commission was unable to ascertain but part of the facts. The testimony obtained was, however, sufficient to incriminate the company in many unlawful acts, among the most important of which were the violation of laws, both Federal and State, in respect to monopolies; the use of the stockholders' money to control legislation, politics, and the press; and the deceptive manner in which the accounts were kept respecting the capital investment and the operating expenses.

An added romantic interest attaches to this report since it includes correspondence between two railroad presidents, who proudly styled themselves "Pizarro" and "Cortez," joyfully imagining they have "subjected the natives" and can now divide the Western Hemisphere between them.

On account of the refusal of certain officials to testify before the commission regarding their acts, an appeal was made to the Supreme Court of the United States, which court, in December, 1917, issued a mandamus directing these witnesses to appear before the commission and testify. When this additional evidence is taken, the result will be to make the investigation of added interest.

As the stories of all the railway systems investigated by the commission are nearly identical and include practically all of the same illegal acts, we will, for lack of space, record only some of the principal features brought out in this case.

The following brief extracts from the commission's report, outlining the history of the road, its accounting as to capitalization, operating expenses, etc., appear in pages 168-173:

METHOD OF THE INVESTIGATION.

On November 10, 1913, immediately following the adoption of the Senate resolution above referred to, the commission ordered an investigation into the questions presented and served formal notice of this investigation upon the carriers concerned. Thereafter examiners of the commission were directed to examine the accounts, records, and memoranda of the Louisville & Nashville Railroad Co. and the Nashville, Chattanooga & St. Louis Railway with a view to securing all information in the files of these carriers that would throw light upon the questions contained in the Senate resolution. Certain obstructions have been placed in the way of the commission's

examiners by the carriers, and these will be referred to later. The facts stated herein were secured from the annual and statistical reports and the contracts and tariffs on file with the commission, from such of the carriers' records and accounts as were voluntarily submitted by them; from testimony given at formal hearings in other cases before the commission; and in a few cases, that will be indicated, from interviews by the commission's examiners with railroad officials and other persons. The questions presented by the resolution will be stated and answered in numerical order, accompanied by such comment as seems necessary. Following the report will be found an appendix illustrating and supplementing certain of the answers.

INTEREST OF THE LOUISVILLE & NASHVILLE RAILROAD CO. IN OTHER RAILROADS.

The Louisville & Nashville Railroad Co. was incorporated in Kentucky in 1850. The line from Louisville to Nashville, 185.81 miles in length, was completed and placed in operation in 1859, forming the nucleus of the present system. Various extensions have since been constructed aggregating 399.56 miles, and making a total of 585.37 miles constructed by the company under its own charter. The annual report of this carrier to its stockholders of the year ended June 30, 1913, shows that it owned or controlled on that date 7,889.77 miles of road. A comparison of the miles of road constructed by this company under its own charter with the total miles of road owned or controlled by it well illustrates its activity in securing control of other railroads.

The several lines acquired by the Louisville & Nashville through purchase, lease, control, or otherwise, together with the dates of acquisition and the length of each, are listed under appropriate captions in Appendix A to this report.

COST OF ROAD.

Before the Louisville & Nashville advised the commission that such of its records as were made prior to August 28, 1906, would not be submitted for inspection, schedules of most of the cost of road accounts had been drawn from the ledgers preparatory to completing the analysis of the accounts from information to be secured from the journals and other records of original entry. While a complete analysis of these accounts was prevented by the Louisville & Nashville the preliminary analysis was sufficient to indicate that the cost of road account is heavily burdened with charges which do not represent actual construction cost. From such incomplete information it is concluded that at least \$16,000,000 shown in the cost of road accounts covers items which should not be charged as a part of the cost of this carrier's road, as follows:

Charges included in cost of road accounts but not expended for actual construction.

Discount on stock.....	\$1, 440, 018. 00
Other expenses in connection with the sale of stock.....	32, 671. 48
Discount on bonds.....	2, 192, 142. 57
Other expenses in connection with the sale of bonds.....	8, 537. 95
Interest and dividends.....	1, 917, 535. 13
Amounts credited to profit and loss:	
For reasons not stated.....	\$2, 640, 000. 00
To provide a surplus in order that a stock dividend of 100 per cent might be paid.....	6, 300, 000. 00
To raise book value of stock above the actual cost of acquirement.....	1, 422, 784. 00
To adjust difference between advances made for construction and par value of bonds received in settlement therefor.....	78, 447. 72
	<hr/> 10, 441, 231. 72
	<hr/> 16, 032, 136. 85

The above statement is illustrative of the character of charges which the carrier has included in its cost of road account. A full examination of the carrier's accounts might disclose conditions under which some of the above amounts could properly be charged to cost of road account, but it is also possible that other improper items would be found which would greatly augment the amount shown.

Stock and dividends of 100 to 200 per cent declared and excessive charges made to property account.—The extracts referring to the above subjects are taken from pages 171–173 of the commission's report.

STOCK DIVIDENDS DECLARED.

As shown in the above table, a stock dividend of 100 per cent was declared by the Louisville & Nashville on October 6, 1880. According to a corporate history of this railroad, which was found in its office, 10 stock dividends were declared by this company between 1860 and 1891.

* * * * *

To make possible the stock dividend of 100 per cent declared on October 6, 1880, the amount of surplus was arbitrarily increased by raising the book value of certain assets. From the corporate history above referred to it appears that when this dividend was declared the book value of the carrier's property exceeded its capital stock liability.

* * * * *

To meet this situation the assets of the company were revalued, and the board of directors voted that the book value of certain assets should be increased. Accordingly entries were made on the books of the company crediting the profit and loss account and correspondingly increasing the book value of the following assets in the amounts shown below to \$7,212,226.

The above-mentioned entries brought the profit and loss account to \$10,883,609, to which was charged the 100 per cent dividend of \$9,065,000.

The above facts illustrate the manner in which permanent improvements on the Louisville & Nashville have in the past to a large extent been made out of earnings and subsequently charged to the capital account. As the commission in its annual reports has previously pointed out, only by the fullest publicity and public supervision of stock and bond issues may such increasing of the capital accounts of carriers at the expense of the public be prevented.

EXCESSIVE CHARGES TO PROPERTY ACCOUNT.

The issued capital stock of this carrier amounts to \$16,000,000, par value, of which \$15,984,787.50, par value, is outstanding. It appears that cash aggregating only about \$9,831,840.77 was received for this stock, while an amount exceeding \$8,107,398.50 was given to stockholders in the form of stock dividends and by the sale of stock at prices below par and also below market value. Included in this amount is a stock dividend of 200 per cent on the outstanding capital, which was authorized by the board of directors on August 10, 1873. The dividend as originally declared amounted to \$4,324,032.96, which was charged to the carrier's property investment account on July 31, 1873, as an offset to the carrier's liability for stock issued from which no funds were derived. Later the dividend was increased \$251,671.79, which amount, however, was not charged to property investment but to profit and loss. Of this amount \$181,537.33 was recorded in the books by an entry dated June 30, 1875, and represented the dividends of 200 per cent on \$91,201.44 of capital stock held in the treasury.

*How the directors spent large sums of the stockholders' money to control the press, politics, and legislation and to influence public sentiment, for which purpose they formed the "Tennessee Railroad Association"; other "fake" organizations for the same purpose were formed.—*The following extracts are from pages 229 to 233 of the report:

EXPENSES FOR THE PURPOSE OF MAINTAINING POLITICAL AND LEGISLATIVE AGENTS

Expenditures by the Louisville & Nashville during this period which appear to have been for the purpose of maintaining political and legislative agents amounted to \$23,274.41. This amount was distributed as follows:

Expenditures for securing copies of and information concerning legislative bills of particular interest to the Louisville & Nashville.....	\$1, 413. 58
Expenditures directly assignable to specific legislation.....	5, 596. 60
Contributions to various committees or associations for the purpose of influencing legislation.....	6, 611. 29
Expenditures on account of legislative agents in general.....	9, 652. 94

FOR THE PURPOSE OF INFLUENCING PUBLIC SENTIMENT.

The accounts of the Louisville & Nashville disclose that between September 1, 1906, and July 1, 1914, this carrier expended at least \$59,322.48 for the purpose of creating public sentiment in favor of its plans.

Of this amount, over \$53,000 was spent in a publicity campaign in Alabama in the endeavor to mold public opinion through the medium of the press. Part of the

balance was contributed by the Louisville & Nashville to a fund made up by numerous carriers to finance a campaign in Louisiana to prevent the change of tax laws. In order that the railroads concerned might preserve an outward appearance of indifference in regard to the legislation in question, the contributions for this purpose were placed in the hands of a bank to be disbursed by it as if in furtherance of banking interests. If the commission's examiners had been accorded access to the correspondence files of this carrier and to its accounts prior to 1906, there seems no doubt that information as to other substantial expenditures for the purposes referred to in the question would have been secured.

TENNESSEE RAILROAD ASSOCIATION.

The Louisville & Nashville was one of the railroads which about 1884, for the purpose of combating adverse legislation in Tennessee, formed the Tennessee Railroad Association.

A large number of vouchers, aggregating, between September 1, 1906, and July 1, 1914, approximately \$295,000, were issued by this carrier to various persons, as to which the accounts contained no information other than that the expenditures were for "special" services and expenses. Although a number of these vouchers bore the notation "as per statement on file in the general manager's office," a request that such files be submitted for inspection was denied.

Numerous other vouchers issued between September, 1906, and July, 1911, and aggregating \$67 722.30, are recorded as having been issued under the direction of the legal or executive departments without the purpose being stated. These were for amounts in excess of \$1 000—one such voucher, made in February, 1910, is for \$20 715.06. Whether such sums were spent for the purposes referred to in the question can not be determined.

The character of some of the special ledger accounts recording large expenditures, the purpose of which could not be learned from the accounts is outlined below:

An account was opened in the name of the Immigration & Industrial Association of Alabama in January, 1907. This records cash advanced to George W. Jones, assistant district attorney at Montgomery, Ala., made under the authority of the first vice president; \$13 068.80 was charged to this account; \$7,868.86 was re-collected from other carriers who were parties to the association and credited to this account. The balance of \$5 199.94 remaining was charged to operating expenses by authority of the first vice president. The nature of this account is indicated by notations on the treasurer's statements of cash receipts entered therein, such as "proportion of expenses account adjourned session of Alabama Legislature."

The above are illustrative of numerous suspense accounts opened prior to 1913 in which the entries were of such a vague character as not to disclose the purposes for which they were kept. Under the accounting rules prescribed by the commission the keeping of such vague accounts at the present time would subject the carriers to prosecution.

In the testimony taken during these investigations by the commission, which is printed in a volume of 519 closely printed pages (S. Doc. No. 461, 64th Cong., 1st sess., 1916), over 150 pages of testimony appear in reference to the bribing of legislators, chiefly through passes, which aggregated over 7,000,000 miles of free transportation. These passes were accepted by governors and in many cases by judges, as well as by more than 90 per cent of the members of the legislatures of the various States through which the lines passed. That these passes were understood by the legislators as bribes is clearly shown in letters where they promise the railway officials to "give them whatever they wanted" in return for the passes. An interesting letter is one introduced in the evidence, in which the writer addresses the railway official as "Dear Bribe Giver:"

[J. A. Clement, lawyer, suite 11-12 Baker Building.]

DICKSON, TENN., October 7, 1915.

Mr. D. G. HUDSON,
Nashville, Tenn.

DEAR BRIBE GIVER: You promised me Saturday you would send pass for Mr. C. from Dickson to Nashville and return, Monday, but you overlooked your hand again. Luke must have you thinking. Please send it by the 2.15 train to-morrow, if possible.

* * *

Yours truly,

J. A. CLEMENT.

Division of two continents.—Having subjugated the American citizens, as they thought, as did Cortes and Pizarro of old, two railroad presidents proposed to divide the Western Hemisphere between them. Some of the most interesting testimony, bordering upon the romantic days when Pizarro and Cortes subjugated the natives of the Western Hemisphere about four centuries ago, is to be found in the testimony of two railroad presidents who having, as they thought, secured the subjection of the present American people as did those plunderers of old, felt the time had arrived when they could enjoy the realization of their further dreams of conquest and accordingly, under the names of "Pizarro" and "Cortez," Milton H. Smith, president of the Louisville & Nashville Railway System, and Samuel Spencer, president of the Southern Railway, gave vent to their feelings of pride and joy in some very interesting correspondence, to be found in the testimony taken by the commission and published as Senate Document 461, Sixty-fourth Congress, first session, entitled "Louisville & Nashville Railway Company Hearings Before the Interstate Commerce Commission," 1916. This correspondence, exemplifying the illimitable ambitions of railway financiers, is of great interest. The following extracts from the testimony of President Smith and the letters referred to appear on pages 369 to 372 of the document.

A letter from President Smith, of the Louisville & Nashville Railroad, to President Spencer, of the Southern Railway:

[Personal and confidential.]

ON PENNSYLVANIA RAILROAD TRAIN No. 21,
February 22, 1896.

SAMUEL SPENCER, Esq.,

President Southern Railway, 60 Broadway, New York City.

DEAR SIR:

PIZARRO. How shall we divide the new world?

CORTEZ. I will take North America and you can have all of South America, except ———, and neither of us will do anything to the Isthmus without notice to and cooperation of the other.

PIZARRO. While Patagonia is not a very large or important part of the world, yet, perhaps, it is as much as I can tote.

Refer to typewritten report of our interview at Kenesaw, Ga., on October 28, 1894, and to the interviews and correspondence that have taken place since that date, and to that portion of our interview of this morning relating to the future of certain railroads that are or may be tributary or competitive with roads controlled by the L. & N. R. R. and the Southern Ry.

May it not be well to review the subject and perhaps make our understandings more specific?

Your affairs, since our interview in October, 1894, progressed with rapidity, and without, so far as I know, encountering serious difficulties. You have acquired the G. S. & F., the Atlanta & Florida, and the Central Railroad has been reorganized in accordance with your plans. I do not recall now what has been done with the Macon & Northern, nor what has been done with the G. M. & G., Macon & B'ham, and one or two other roads, although I believe you told me that your intention was to allow the Macon & B'ham to be abandoned. The Paducah, Tenn. & Alabama and Tenn. Midland Rds. have been disposed of as anticipated. The L. & N. will not compete for the control of the M. & C. Rd. The L. & N. will not compete for the control of the B'ham, Sheffield & Tenn. River Rd., provided you will acquire it, should it become necessary to do so to prevent its extension into Birmingham, or will not permit it to get into a position where it may become a disturber. The L. & N. Rd. will not compete for the control of the Mobile & Birmingham with the expectation that you will acquire it. It is not clear what disposition ought to be made of the Georgia & Alabama Railroad.

* * * * *

I have advised Mr. Belmont of our agreement that neither party will acquire the property of the Marietta & North Georgia Railroad Co. without the consent of the other. You may, therefore, freely communicate with him upon the subject, and I assume he will do likewise.

Yours, truly,

_____, *President.*

Letter from Samuel Spencer, president of the Southern Railway, to M. H. Smith, president of the Louisville & Nashville Railroad Co.:

NEW YORK, February 29, 1896.

MR. M. H. SMITH,
President L. & N. R. R., Louisville, Ky.

DEAR SIR: Your letter of the 22d instant.

Pizarro: Since our last conversation, the division of the New World between us has made some progress.

Cortez: Yes; you seem to have acquired Patagonia, and I have secured a considerable part of North America which touched my former territory, but it seems to me you have acquired a considerable neck of the Isthmus which is the connecting link between us. Was it understood that connecting links which touched both of us should be a matter of consultation before acting or not?

Pizarro: * * * I agreed that it is desirable to renew the subject and, if practicable, to make our understanding more specific. The principles on which I think this understanding should be based are:

(1) That neither the L. & N. nor the Southern, shall acquire lines in the territory of the other, and that lines connecting with or touching one and not the other shall be regarded as in the territory of the one which they connect or touch.

(2) That neither will acquire lines allied by former ownership, lease, or otherwise, to the other, and which at the moment are not controlled by reason of pending reorganizations or other cause.

(3) That neither will acquire lines which connect with or touch both, either directly or through subordinate or controlled lines without previous consultation and, if possible, agreement.

(4) That neither will foster the construction of new lines or the completion of unfinished ones into the territory of the other, but when questions with reference to such lines arise, we shall proceed by agreement with each other, if possible.

Will you please consider this and say if such a declaration of principles is satisfactory?

* * * * *

Confirming our verbal understanding of the 22d instant, I beg to say that we will give no encouragement to the construction of such a line without previous consultation and understanding with you, but if the present projectors, or others, develop sufficient strength to carry the enterprise through from Nashville to Harriman we will cooperate with you on a fair basis as to the handling of any business in connection with it which is competitive with you. I note your advices to Mr. Belmont concerning our agreement that neither party will acquire the property of the Marietta & North Georgia without the consent of the other, and I confirm that agreement.

Yours, very truly,

S. SPENCER, *President.*

The Pere Marquette and Cincinnati, Hamilton & Dayton.—The history of this railroad system in its gross mismanagement, maladministration, and the peculations of the great financiers who wrecked it, is largely a counterpart of the history of the three systems whose rise and fall from power have already been sketched. Time will not permit going into the details of this interesting history, which is replete with startling instances of financial legerdemain. It is interesting to the people of Ohio and Michigan, through which States these lines are chiefly laid, to learn of the pressure which was brought to bear upon the legislatures of these States to increase the rates of charge, on the excuse that they were insufficient to pay legitimate revenue; whereas the investigations of the Interstate Commerce Commission clearly show that the troubles of this railway

system were due entirely to the wild speculation and disregard of the principles of business ethics which are practiced by reputable business concerns.

The following brief extracts are taken from the official report of the Interstate Commerce Commission, No. 6833, dated March 13, 1917, entitled "In re Pere Marquette Railroad Company and Cincinnati, Hamilton & Dayton Railway Company."

INTRODUCTION.

It may be well at the outset to marshal the outstanding facts, among the many disclosed of record, which have affected the ability of these two carriers to do their duty as common carriers and also the value of their securities in the hands of the investing public.

The Pere Marquette came into being as a consolidation of three relatively unsuccessful Michigan roads and began operation on January 1, 1900. The consolidation was brought about by New England interests headed by W. W. Crapo and Nathaniel Thayer, and in the process outstanding capital stock in the hands of the public was inflated by \$1,461,250 and book value of property by \$4,290,230.41. The Crapo-Thayer control continued for three years. Its operating policies were sound in the main; rolling stock and miles operated were increased; a small surplus was accumulated and used for improvements; no common-stock dividends were paid, and physical condition was bettered. Outstanding long-term debt was increased by almost \$6,000,000 and at the end of the three years was about \$31,000,000. In the next 12 years it was increased by more than \$50,000,000 under the succeeding managements.

The first of these was the Prince management, which secured control on December 29, 1902, through purchase of Pere Marquette common at a maximum of \$85 per share. Its policy of expansion included acquisition of new equipment costing over \$6,000,000, and of about 383 miles of main and branch lines, most of which had a history of failure. In acquiring this mileage underlying bonds of over \$4,000,000 were assumed and almost \$3,500,000 bonds issued. The Prince interests reversed the policy of their predecessors, undermaintained road and equipment, paid unearned dividends on common stock, and, in the 18 months of their management, added \$2,500,000 net to current liabilities, also added over \$14,500,000 to outstanding long-term debt, promoted a C., H. & D. syndicate, and through it sold 110,000 shares of Pere Marquette common to the C., H. & D. at \$125 per share.

The next management was that of the C., H. & D. syndicate, which took control of both carriers on July 7, 1904, and parted with it in the following month to the Zimmerman-Hollins interests. During these few weeks new and heavy burdens were bound upon the Pere Marquette.

The Zimmerman-Hollins management succeeded to the control in August, 1904, and continued the work begun by the Prince interests, with the result that when the control of both roads was sold to J. P. Morgan & Co. on October 20, 1905, both were promptly put under the first receiverships which began in December, 1905.

Meantime another \$10,000,000 of long term Pere Marquette securities had been marketed through interested parties at a cost to the road of over \$1,100,000 in discounts, \$1,645,000 was paid to certain members of Hollins's pool for their worthless stock in the Toledo Railway & Terminal Co., \$400,000 was advanced under syndicate schemes to affiliated companies and lost, and over \$1,100,000 was used to pay off floating debts contracted by the Prince régime. The mileage and equipment were somewhat increased. Operation was unsuccessful and resulted in deficits.

Two years of receivership were succeeded in December, 1907, by a Morgan reorganization based on the consolidation of the Pere Marquette with its already controlled Pere Marquette of Indiana, 20 miles long. This furnished the pretext for further stock inflation, for an issue of \$5,000,000 of 6 per cent debentures, and for the writing up as "cost of road and equipment" of the direct losses, aggregating almost \$5,000,000, of the former administrations. Morgan control has continued since, except for the second receivership, which began on April 5, 1912. In the intervening years the Pere Marquette was in constant difficulty, revenues failed to provide for expenses and charges, and bond interest was paid only at the cost of adequate maintenance of the property. Road and equipment deteriorated markedly, financing became more and more difficult, and needed funds were secured only at the expense of heavy discounts. The second receivership was necessary to accomplish what the first had failed to accomplish—the physical and financial rehabilitation of the Pere Marquette.

The road is now emerging from the second receivership. During five years of court control it has greatly improved in physical condition, and its service has improved

accordingly. Under the reorganization plan a large part of the fixed interest-bearing obligations outstanding on June 30, 1916, are to be exchanged for capital stock, of which there is to be \$11,200,000 of 5 per cent prior preference, cumulative, \$12,429,000 of 5 per cent preferred, cumulative, and \$45,046,000 of common shares. The plan contemplates a decrease of over \$8,000,000 in capitalization, exclusive of overdue interest on funded debt amounting to approximately \$10,000,000, and a considerable decrease in fixed interest charges. The new capitalization will also represent \$16,000,000 of new money provided for reorganization expenses, additions and betterments, working capital, and other purposes.

In contrast to the Pere Marquette the C., H. & D., prior to July 7, 1904, when the C., H. & D. syndicate took control, was a highly prosperous road, despite losses of several millions through Henry S. Ives and his associates in the late eighties, the drain of supporting less prosperous lines west of Hamilton, Ohio, a funding of deficits and interest on the western lines into some \$1,800,000 of bonds, and the injection in 1895 of \$10,200,000 of water into the capital stock through the consolidation effected by the Shoemaker-Woodford interests, then in control. These interests sold out to the C., H. & D. syndicate in 1904, receiving \$125 per share for their common stock, which was water, and \$110 per share for 10,000 shares of preferred stock. The surplus of that date was replaced in the following year by a deficit of at least \$1,086,127.49, allowance being made for some \$843,000 concealed by falsification of accounts.

Morgan control, from 1905.—The next important changes came when the control of the C., H. & D., and incidentally of the Pere Marquette, passed to the Erie Railroad Co. Representatives of the Erie took charge of the Pere Marquette management on October 20, 1905. Shortly thereafter upon the rescission of the Erie's purchase of the C., H. & D. from J. P. Morgan & Co., George W. Perkins, of the latter firm, on December 4, 1905, went on the Pere Marquette board and the Erie representatives remained. It appears that Perkins more than anyone else guided the Pere Marquette through the reorganization following the receivership of December 4, 1905.

In discussing the matter of stock control after the first receivership consideration must be given to the reorganization which followed. This "reorganization" of December 11, 1907, was on paper only. The thing accomplished was release of the Pere Marquette from receivership without either foreclosure or a downward adjustment of capital liabilities. The means used as a pretext was merely the consolidation of the Pere Marquette of Michigan with its subsidiary, the Pere Marquette Railroad Co. of Indiana. This subsidiary will be further considered, but note may be taken here that it was only 20 miles long; that its capital stock of \$500,000 was owned by the parent company; that its bonds bore the guaranty of that company; and that it had been constructed, in effect, by the parent company to piece out the latter's line toward Chicago. In this consolidation the name "Pere Marquette Railroad Company" was retained; capital stock, including first and second preferred as well as common, was provided for to the amount of \$28,500,000, equaling the authorized issues of the two constituents; their funded debt and other obligations were assumed; and last, but of great importance, \$5,000,000 of 6 per cent five-year debenture bonds were authorized to take up current indebtedness, including receiver's certificates, and were offered to the stockholders.

The first board of the reorganized company, elected August 12, 1907, was a Morgan board. No changes of consequence occurred in its make-up until November 5, 1909, when certain representatives of the Baltimore & Ohio Railroad Company were elected, following the latter road's entrance into C., H. & D. affairs. But even then the Morgan interest was the dominant one in the Pere Marquette board. Early in 1911, when the C., H. & D.'s 110,000 shares were finally sold to J. P. Morgan & Co., the Baltimore & Ohio directors resigned.

A little more than a year later, on April 5, 1912, the road again went into the hands of receivers. On March 9, 1914, there was another extensive change, with more residents of Michigan on the board.

Passing now to a consideration of the roads "affiliated," it appears that for the Huron & Western, which ran west from Bay City principally to serve a coal mine, the Pere Marquette paid \$106,559.29 to the Grand Trunk Railway system, which seemingly had built it at that cost. At the same time the stock came into the possession of the Pere Marquette, and since 1903 the road has been operated as a part thereof. At the price paid this property cost about \$9,340 per mile.

No accounts of the Grand Rapids, Kalkaska & Southeastern can be found. This line ran from Rapid City, Mich., in a generally southeastern direction, to Stratford, Mich. It was built to connect a timber tract of the Thayer Lumber Co., located in Missaukee County, with the Chicago & West Michigan. This latter road, by contract,

agreed to oversee the construction, furnish the necessary rolling stock, and lease and operate the road for 10 years following its completion, paying as rental \$20,000 per annum plus 15 per cent of gross receipts except upon pine.

Its minute books show that the Kalkaska road was to be constructed by William Alden Smith, under a contract dated October 21, 1897, by which the constructor was to receive as payment \$200,000 in bonds and \$264,000 in stock, less such as had been subscribed by him. According to the State railroad commissioner's reports the entire sum of \$464,000 was treated by that carrier as cost of road and equipment.

In 1903, a few years prior to the expiration date of the lease, the Pere Marquette, through a contract with George A. Fernald and others, purchased the entire capital stock of the Kalkaska road for \$107,000, payable in Pere Marquette consolidated 4 per cent bonds, and assumed its \$142,000 of first mortgage 5 per cent bonds then remaining outstanding. The result was a standing minimum fixed charge against the Pere Marquette of \$11,380 annually for what was originally a tap line and undoubtedly diminishing in value as the timber was being cut out. Speaking of this branch in May, 1915, the chief operating officer of the Pere Marquette said:

"It is bad. There are 14 miles of the track from Eastman Junction to the end at Stratford that is so bad that we operate it under caution, and I am about to ask the railroad commission for the authority to take it up. There is no business on the branch. to warrant our continuing in operation, and we are now going up there twice a week to bring out what little business there is."

* * * * *

Morgan's purchase was on behalf of the Erie Railroad Co. The incidents of that purchase, its speedy rescission by the Erie, and the assumption by Morgan of the obligation, are later set forth. Immediately after the control had been returned to Morgan a receivership was asked, and it began December 4, 1905.

* * * * *

VIII. MORGAN MANAGEMENT, FROM 1905.

It seems proper to treat these years as one period in the history of the Pere Marquette. During this period there were extensive changes in the stock ownership, particularly in the transfer of the C., H. & D. holdings of 110,000 shares of Pere Marquette common to J. P. Morgan & Co., and there were changes in the Pere Marquette directorate as a result of the purchase of control of the C., H. & D. first by the Erie and then by the Baltimore & Ohio, while the C., H. & D. still held that common. But from December 4, 1905, when George W. Perkins went on the Pere Marquette board, representing Morgan & Co., that firm seems at all times to have been the guiding hand in Pere Marquette affairs.

The first event of importance, following the acquisition of C., H. & D. control by the Erie on October 20, 1905, and the reorganization in its interest of the Pere Marquette board, was the receivership under Judson Harmon, commencing December 4, 1905. This was coincident with the receivership of the C., H. & D., and on behalf of Morgan & Co. it is insisted that the step was necessary in order to separate the two corporations. However that may be, it is apparent that the Pere Marquette of itself was then well on the way toward a receivership. It continued under a receiver until December 14, 1907.

The losses to the stockholders under Morgan control exceed \$22,000,000.—
The following is from page 59 of the commission's report:

Through this Morgan reorganization the Pere Marquette emerged from receivership in 1907 carrying a load of outstanding capital stock and funded debt heavier by \$7,000,000 than that under which it was staggering when the receivership began two years before. It never succeeded in carrying itself thereafter. A proper reorganization would have included reduction and not increase of fixed charges. The plan of reorganization dated October 30, 1916, carries marked decrease in fixed charges.

Other losses carried through the profit and loss account in addition to the results of operation must be considered. In the aggregate the showing to June 30, 1914, was as follows:

Debits:	
Net loss from income.....	\$12,962,905.48
Debt discount extinguished.....	10,500,486.02
Net loss on retired road and equipment.....	3,054,800.59
Miscellaneous debits.....	724,047.40
Total debits.....	27,242,239.49
Credits: Miscellaneous credits.....	5,187,199.76
Profit and loss balance (deficit).....	22,055,039.73

Falsification of accounts.—Under the above heading the commission reports in detail certain accounts which proved to be false, respecting which they make the following remarks:

12. *Falsification of accounts during Zimmerman-Hollins control.*—The following statement presents a condensed income account covering the year ended June 30, 1905, for the C., H. & D., including its proprietary line, the Cincinnati, Indianapolis & Western, 1,038.24 miles operated, as recorded in the carrier's books of account:

Gross earnings from operation.....	\$6,008,917.65	
Operating expenses.....	8,095,885.11	
Income from operation.....		\$1,913,032.54
Taxes.....		316,061.12
Net income from operation.....		1,596,971.42
Income from other sources.....		59,688.65
Gross income.....		1,656,660.07
Deductions from gross income:		
Rents paid for lease of road.....	\$517,288.35	
Miscellaneous rents.....	372,273.11	
Interest accrued on funded debt.....	1,009,515.63	
Other deductions.....	348.52	
Total deduction from income.....		1,899,425.61
Net deficit.....		242,765.54

The 4 per cent preferred stock bore guaranteed dividends, which makes the accrual of the dividend more in the nature of a fixed charge than a division of profits. If these dividends are so considered, the net deficit for the year was \$251,969.20.

The foregoing income account bore little resemblance to the truth. The fact is that large sums properly chargeable to the income for 1905 were ordered to be charged to various other accounts and were so charged in a way to conceal the true state of the company's affairs. These entries violated commonly accepted accounting principles in such a flagrant manner as to make it evident that the purpose was to deliberately falsify the accounts in an effort to avoid showing the utter failure of the company to earn anywhere near its fixed charges.

The charges against the income of that year thus willfully omitted included interest on loans made to retire preferred stocks; interest

* * * * *

But what the Zimmerman-Hollins management accomplished along that line was little compared with what it attempted.

On pages 161-162 are the following, showing how false and "fake" telegrams were used:

Further, in connection with this financial statement, on which such great reliance was placed, we must refer to an exchange of correspondence which occurred between August 15 and 24, 1905, concerning a certain statement then being prepared at the direction of the Hollins firm by President Zimmerman, and one copy of which eventually went to that firm and another to George W. Young. This statement is described in the correspondence as one showing "capitalization, fixed charges, estimated earnings, etc., of the C., H. & D. and P. M.," the figures for the Chicago, Cincinnati & Louisville to be omitted, and this description fits well the document placed in this record on behalf of J. P. Morgan & Co. It was prepared in and forwarded from Cincinnati by N. B. Hersloff, an employee of Hollins & Co., but evidently did not show as favorable results as were desired, for on August 24 the firm wired Zimmerman as follows:

"Better not have Young show statement you sent him; estimate earnings too poor; telegraph him in two separate telegrams, one not use statement sent him, as you have another corrected one, and another telegram saying have not mailed statement because will bring on figures with me early next week."

One of the startling disclosures in this investigation is the ease and informality with which one man, in a leisure hour at his home, can, on a sheet of note paper, either buy or sell a great railroad, as happened in the case of the Pere Marquette. After referring to

instances of the maladministration of this system, showing losses of the stockholders of about \$16,000,000, the following story of the sale of this system is found in the report of the Interstate Commerce Commission, on page 166:

What had happened in the 24 hours meanwhile was that J. P. Morgan and H. B. Hollins had met at the former's New York residence on September 9, 1905, and closed an agreement for the purchase by Morgan of Hollins's C., H. & D. stock holdings, involving an expenditure of some \$12,000,000. Francis Lynde Stetson was present as Morgan's counsel and wrote the agreement on a sheet of note paper. Its text follows and its significance will be further considered:

9 Sept. 1905.

219 MADISON AVENUE.

H. B. Hollins & Co. will sell and J. P. Morgan & Co. will purchase 56,000 shares of C. H. & D. R. R. Co. Common Stock at the price of 160% with interest at the rate of 4½% per annum from December 7th, 1905, until date of delivery, all dividends to be credited against the interest and to J. P. Morgan & Co.

This delivery may be made by H. B. Hollins & Co. at any time, and must be made by them upon October 1st, 1906, or at such time thereafter as shall be specified by J. P. Morgan & Co. by three months' notice in writing.

If so requested by H. B. Hollins & Co., J. P. Morgan & Co. will lend to them upon their obligations secured by C. H. & D. stock or syndicate subscriptions at 135% such sums as they may find necessary to carry such stock or subscriptions, to an aggregate amount not exceeding 56,000 shares, the rate of interest to be 4½%.

This contract and all obligations of J. P. Morgan & Co. may be terminated by them at any time after October 1, 1906x, by three months' notice in writing by J. P. Morgan & Co.

J. P. MORGAN & CO.
H. B. HOLLINS & CO.

x1906

H.B.H.

J.P.M.

*In addition we gave H. B. H. & Co. order to buy about 16,000 sh. participation ctf's. at about 135.

* * * * *

In working up this new syndicate it seems that all concerned were informed as to the true financial condition of the properties, so that it would appear to have been a difficult matter to induce subscribers to embark in the new venture. Even though certain of the obligations were recapitalized so as to reduce the fixed charges to the level of the earnings, as seems to have been proposed, the proposition would still seem to have been too uncertain to attract such substantial subscriptions as were needed. It may well be that the following sentence from Erb's letter of September 20, 1905, addressed to one of the original subscribing interests of May 19, 1904, suggests one, if not the underlying, purpose of this syndicate:

"Messrs. Edwin Hawley and John W. Gates were unimportant participants in this syndicate and their names were made use of, with J. Pierpont Morgan & Co., to create the impression that the property would go into speculative hands, and they have since stepped forward to take the property from Messrs. H. B. Hollins & Co., thus relieving the entire situation and to the satisfaction of everybody in interest."

Whatever motive lay beneath the new syndicate scheme, there is no doubt as to the effect it had on the Erie management.

* * * * *

Mr. Harriman is introduced in the transaction and the president of the Erie Railroad is snubbed by Mr. Morgan.—The following is from pages 172-173 of the report:

President Underwood's reference to Harriman's whereabouts prior to their interview arose from a question as to the accuracy of a report that the Erie's purchase of the C., H. & D. had transpired during Harriman's absence from the country. This record does not settle this point definitely, but it does show that Harriman did not attend any meeting of the board or executive committee during the period July 26 to November 1, 1905. The record also clearly indicates Harriman's emphatic disapproval of

the purchase upon his return in November, with the result that President Underwood obtained another interview with Morgan, as to which he testified as follows:

"Then I went down and had an audience with Mr. Morgan, and I told him that practically the C., H. & D. had a floating debt that was not visible and in the statement he showed me. He said: 'Well, we will look at the statement,' and there was some attempt made to find that statement, but it was unsuccessful; it was not produced. I had not kept it because—well, I did not keep it. I said: 'Mr. Morgan, the statement that I made to you of the effect that the acquisition of the C., H. & D. on the Erie's finances is null and void, because the statement was inaccurate.' He looked at me and said: 'Well, sir, if the statement that we made to you was inaccurate, and for any reason you think that the Erie Railroad has made a bad trade, your duty is very simple—you have only to convene your board of directors and rescind it, and I advise you to do it at once.'

"I bade him good afternoon and walked out of his office, and as I came out of his office I met Mr. Stetson, and I told him, being counsel, 'Mr. Morgan has just authorized the rescinding of that trade, and I think it was a very unusual and extraordinary thing for him to do. I am surprised that he would do it. And I wonder if it would be bad taste for me to tell him that.' He said: 'He might like to hear it.' So I went back, and Mr. Morgan was standing with a paper in his hand, and I said, 'I would like to speak to you for a minute.' He made no answer. I said again, 'I would like to speak to you for a minute.' I said, 'I want to tell you I think you have done a very big thing, the biggest thing I ever came in contact with.' He said nothing. I said, 'Did you hear me?' He said 'I did, sir.' And I walked out."

In closing the report the Interstate Commerce Commission says as follows:

Nothing disclosed in the record before us is to be more regretted than the readiness of great banking institutions in our financial centers to loan enormous sums of money upon exceedingly precarious security in aid of such schemes as have been devised in the wrecking of these railroads. Not only this, but the high officers of such institutions, while acting ostensibly as directors of the railroads, have in fact been little more than tools and dummies for the promoters. The trustees of other people's money seem to have had little compunction about violations of their trusts for the benefit of the promoters, and at their demand.

Can the like of what has befallen these two roads be made impossible hereafter? Perhaps not entirely, so long as financial circles continue complaisant toward financial exploitations which prove successful. But it will help if minority stockholders are more watchful of their interests and if bondholders assert their rights before their security fades away for lack of upkeep, purposely neglected in order to pay interest and dividends unearned. It would, in our opinion, render such exploitation more difficult if the issuance and marketing of all securities of common carriers were subject to Federal regulation. As to that we renew the recommendations repeatedly made to the Congress in our annual reports. We also point to the lesson, here again taught, that access to correspondence files is indispensable for a thorough and accurate understanding of the motives and purposes which underlie the formal entries made in accounts and records.

Unwise management contributed to the downfall of these roads, but breach of trust by corporate officials, often for personal gain, was the main cause here, as in the records developed in other investigations. Consolidations and Combinations of Carriers, 12 I. C. C., 277; The New England Investigation, 27 I. C. C., 560; St. Louis & San Francisco Railroad Investigation, 29 I. C. C., 139; Financial Investigation of N. Y., N. H. & H. R. R. Co., 31 I. C. C., 32; Financial Transactions C., R. I. & P. Ry. Co., 36 I. C. C., 43. That downfall, with its deplorable consequences, can be traced only to betrayal within, and not to compulsion from without. Neither rivalry, nor rate level, nor regulation, nor all combined, can be found on this record to have contributed in any appreciable degree to the disaster.

In discussion of transportation conditions during the last two years or more much has been made of the fact that over 40,000 miles of our railroads were under receivership. A recent publication lists 69 railroads, among them the Pere Marquette and C., H. & D., as in the hands of receivers on December 31, 1916. Their combined operations cover 34,559 miles. Over 40 per cent of that mileage is in systems which, as shown by our investigations, have suffered principally from financial mismanagement and exploitation. Over 40 per cent more, of which a large part is located in Texas, is comprised in two southwestern systems. The remaining 5,800 miles are distributed among fifty-odd carriers in different parts of the country.

The statements of fact herewith presented having all been verified from the official records and sworn testimony taken before the Interstate Commerce Commission, disclose a condition of profligacy, waste, falsifying and destruction of records, and the ignoring and violation of law, both State and National, so vast in its conception and so successfully carried out in defrauding the American people as to be beyond belief.

Can it be possible that the American people, after learning how our great governmental functions have been usurped by the few, who have been given such vast and dangerous powers by special privilege, will permit this "invisible government" to destroy democracy and the public welfare in our Republic as here disclosed? The record is before you and the only remedy lies in the ownership by the people and the operation through the agencies of their Government of all those utilities and natural resources which by right belong to the people, and upon the just and democratic administration of which the public welfare and happiness depend.





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